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Exchequer Court of Canada

RALPH M. SPANKIE, Q.C.

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JUDGES

OF THE

EXCHEQUER COURT OF CANADA

During the period of these Reports:

PRESIDENT:
THE HONOURABLE JOSEPH T. THORSON
(*Appointed October 6, 1942*)

PUISNE JUDGES:
THE HONOURABLE J. C. A. CAMERON
(*Appointed September 4, 1946*)
THE HONOURABLE JOHN DOHERTY KEARNEY
(*Appointed November 1, 1951*)
THE HONOURABLE JACQUES DUMOULIN
(*Appointed December 1, 1955*)
THE HONOURABLE ARTHUR LOUIS THURLOW
(*Appointed August 29, 1956*)
THE HONOURABLE CAMILIEN NOEL
(*Appointed March 12, 1962*)
THE HONOURABLE ANGUS ALEXANDER CATTANACH
(*Appointed March 27, 1962*)

DISTRICT JUDGES IN ADMIRALTY OF THE EXCHEQUER COURT OF CANADA

The Honourable W. ARTHUR I. ANGLIN, New Brunswick Admiralty District—appointed June 9, 1945.
His Honour HAROLD L. PALMER, Prince Edward Island Admiralty District—appointed August 3, 1948.
The Honourable SIR BRIAN DUNFIELD, Newfoundland Admiralty District—appointed May 9, 1949.
The Honourable HENRY ANDERSON WINTER, Newfoundland Admiralty District—appointed May 9, 1949.
His Honour VINCENT JOSEPH POTTIER, Nova Scotia Admiralty District—appointed February 8, 1950.
The Honourable ARTHUR IVES SMITH, Quebec Admiralty District—appointed June 16, 1950.
The Honourable ROBERT STAFFORD FURLONG, Newfoundland Admiralty District—appointed October 8, 1959.
The Honourable DALTON COURTWRIGHT WELLS, Ontario Admiralty District—appointed January 28, 1960.
His Honour JAMES AUGUSTIN MACDONALD, Prince Edward Island Admiralty District—appointed July 11, 1961.
The Honourable THOMAS GRANTHAM NORRIS, British Columbia Admiralty District—appointed September 28, 1961.
The Honourable GEORGE ERIC TRITSCHLER, Manitoba Admiralty District—appointed October 19, 1962.

DEPUTY JUDGES IN ADMIRALTY OF THE EXCHEQUER COURT OF CANADA

The Right Honourable JAMES L. ILSLEY, Nova Scotia Admiralty District—appointed November 3, 1958.
His Honour GEORGE LIVINGSTON CASSADY, British Columbia Admiralty District—appointed June 28, 1962.

SURROGATE JUDGE IN ADMIRALTY OF THE EXCHEQUER COURT OF CANADA

ALFRED S. MARRIOTT, Q.C., Ontario Admiralty District—appointed February 21, 1957.

ATTORNEY-GENERAL OF CANADA:
The Honourable EDMUND DAVIE FULTON, Q.C.
The Honourable DONALD METHUEN FLEMING, Q.C.

SOLICITOR GENERAL OF CANADA:
The Honourable WILLIAM JOSEPH BROWNE

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10. *Minister of National Revenue v. Begin, Charles Auguste* [1962] Ex.C.R. 159. Appeal pending.
11. *Minister of National Revenue v. John Colford Contracting Co. Ltd.* [1960] Ex.C.R. 433. Appeal dismissed.
12. *Minister of National Revenue v. Orlando, Mary* [1960] Ex.C.R. 391; [1962] S.C.R. 261. Appeal allowed in part.
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Westminster Bank v. Inland Revenue Commissioners	[1958] A.C. 210	155
White v. The Ship *Frank Dale*	[1946] Ex.C.R. 555	18
Wilson v. Minister of National Revenue	[1960] Ex.C.R. 205	372
Winslow Marine Ry. & Shipbuilding Co. v. The Ship *Pacifico*	[1924] Ex.C.R. 90	452
Winthrop Chemical Co. Inc. v. Commissioner of Patents	[1948] S.C.R. 46	236, 239
Wiseburgh v. Domville	[1956] 1 All E.R. 754	181, 411
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CASES

DETERMINED BY THE

EXCHEQUER COURT OF CANADA

AT FIRST INSTANCE

AND

IN THE EXERCISE OF ITS APPELLATE JURISDICTION

BETWEEN:

1961
June 7, 8
Sept. 19

THE REPUBLIC OF CUBA (a party interested) ..... } APPELLANT;

AND

FLOTA MARITIMA BROWNING DE CUBA, S.A. (*Plaintiff*) ..... } RESPONDENT;

AND

THE STEAMSHIP *CANADIAN CONQUEROR*, THE STEAMSHIP *CANADIAN HIGHLANDER*, THE STEAMSHIP *CANADIAN LEADER*, THE STEAMSHIP *CANADIAN OBSERVER*, THE STEAMSHIP *CANADIAN VICTOR*, THE MOTOR-VESSEL *CANADIAN CONSTRUCTOR*, THE MOTOR-VESSEL *CANADIAN CRUISER* re-named *CUIDAD DE DETROIT* .....DEFENDANTS.

Shipping—International law—Sovereign immunity—Vessels in Canadian port sold to Republic of Cuba—Vessels arrested on behalf of private suitor—Impleading foreign sovereign state.

Banco Cubano del Commercio, a Cuban corporation, in August, 1958 purchased at Montreal eight steamships then lying in the Port of Halifax. On the same date it signed a lease-purchase agreement with the respondent, another Cuban corporation, which provided for the operation of the ships by the latter with an option to purchase. On October 31, 1958 the respondent, claiming the bank had repudiated delivery and usurped its rights under the contract, declared it a nullity and

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surrendered possession of the ships to an agent of the bank but reserved the right to claim damages for breach of contract. On June 9, 1959, the bank sold the ships to the Republic of Cuba. On August 4, 1960 the respondent instituted proceedings *in rem* in the Nova Scotia Admiralty District by a writ directed to the owners and all others interested in the defendant vessels and applied for and was granted a warrant for the arrest of the vessels still in Halifax. Counsel for the appellant entered an appearance under protest on the ground that the court had no jurisdiction and moved to set aside the writ and the warrant for arrest and service thereof on the grounds the vessels were public national property of and in the possession of the Republic which could not be impleaded; and further that by the agreement relating to the use and hire of the ships the respondent expressly submitted itself and all questions relating to the agreement to the jurisdiction of the Cuban courts. Pottier D.J.A. dismissed the application. On an appeal to this Court

Held: That having regard to the nature of the appellant's claim to the ownership of and rights of possession and control in the defendant vessels the Republic of Cuba was in fact impleaded and was intended by the respondent to be impleaded. *The Cristina* [1938] A.C. 485 at 492.

2. That a foreign government, claiming that its interest in property will be affected by a judgment in an action to which it is not a party and in which it alleged it is indirectly impleaded, is not bound as a condition of obtaining immunity to prove its title to the interest claimed, but it must produce evidence to satisfy the court that its claim is not merely illusory, nor founded on a title manifestly defective. *Juan Ysmael & Co. Inc. v. Indonesian Government* [1955] A.C. 72, applied.

3. That on the evidence the appellant's claim to ownership and right of possession of the defendant vessels is not illusory nor founded on a title manifestly defective.

4. That the defendant vessels on August 4, 1960, were the property of the Republic of Cuba.

5. That the rule of sovereign immunity extends to property of a foreign sovereign or state even if that property be used for commercial purposes. The rule as stated by Lord Atkin in *Compagnia Naviera Vasconcgado v. S.S. Cristina* [1938] A.C. 485 at 490, applied.

6. That the Court having come to the conclusion that conflicting rights have to be decided in relation to the claim of the Republic of Cuba, the writs and warrants of arrest and service thereof must be set aside as the Court is without jurisdiction to entertain the action. *Juan Ysmael & Co. Inc. v. Indonesian Government (supra)* followed.

APPEAL from a decision of the District Judge in Admiralty for the Nova Scotia Admiralty District.

The appeal was heard before the Honourable Mr. Justice Cameron at Halifax.

Donald McInnes, Q.C. and *J. H. Dickey, Q.C.* for appellant.

G. S. Black and *D. S. Kerr* for respondent.

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

CAMERON J. now (September 19, 1961) delivered the following judgment:

This is an appeal from a decision of Pottier, J., District Judge in Admiralty for the Nova Scotia Admiralty District, dated April 25, 1961, dismissing a motion made by the Republic of Cuba to set aside the writ and warrant of arrest in this action, and service thereof, on the ground that the Court was without jurisdiction to entertain the action.

On August 4, 1960, the respondent (hereinafter called Flota) instituted proceedings *in rem* in the Nova Scotia Admiralty District against the seven vessels named as defendants, the writ being directed to "the owners and all others interested in the defendant vessels". Its claim was stated as follows:

> The Plaintiff claims against the Defendant vessels the sum of one million, five hundred thousand dollars ($1,500,000) for injury, loss and damage sustained by the Plaintiff by reason of the breach of a Lease-Purchase Agreement (being an agreement relating to the use and hire of ships and relating to the Defendant vessels and others) dated on or about the 19th day of August, A.D. 1958, and for costs, and the Plaintiff claims to have an account taken.

On the same date, counsel for the respondent applied for and was granted a warrant for the arrest of the said seven vessels and they were immediately arrested at the Port of Halifax, Nova Scotia. On August 11, 1960, Mr. McInnes, of counsel for the Republic of Cuba, entered an appearance for Cuba, said appearance being under protest on the ground that the Court had no jurisdiction to entertain the action. Shortly thereafter, Mr. McInnes moved before the District Judge in Admiralty for an Order setting aside the writ, the warrant for arrest, and service thereof on the following main grounds:

(*a*) that the said steamships and motor vessels Defendants herein were and are public national property of and in the possession of and public use and service of the Government of the Republic of Cuba at all times relevant to these proceedings, and cannot be impleaded in this action,

(*b*) that the Lease-Purchase Agreement referred to in the statement of claim herein as an agreement relating to the use and hire of ships is an agreement whereby the Plaintiff expressly submitted itself and all questions relating to the said Agreement to the jurisdiction of the competent Judges and Courts of the Republic of Cuba renouncing their right to resort to any other jurisdiction

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by reason of nationality or of domicile or for any other cause whereby this Court is without jurisdiction and the Plaintiff herein is estopped from resorting to the jurisdiction of this Court.

The Learned District Judge in Admiralty dismissed the said application and an appeal was immediately taken to this Court.

It will be convenient to set out at once certain facts which are not in dispute. The Banco Cubano del Comercio Exterior (Cuban Bank of Foreign Commerce), which I shall hereinafter refer to as Banco, was incorporated in Cuba in 1954, one of its objects being to promote foreign trade by ownership of vessels. Browning Lines, Inc. is a Michigan corporation in the business of owning and operating vessels, its majority shareholders being Troy H. Browning and Lorenzo D. Browning, both citizens of the United States. The Browning Brothers were approached by the Director General of Banco with the view of having them operate vessels owned by Banco. As a result, Flota—the respondent herein—was incorporated under the laws of Cuba on April 8, 1958, its main purpose being the operation of vessels owned by Banco. All of the shareholders of Flota, with one exception, are said to be citizens of the United States.

On May 3, 1958, Flota entered into a Lease-Purchase Agreement with Banco relating to the operation of six vessels owned by or being built for Banco in England and Japan. That was at times referred to as the English contract. Shortly thereafter, the Browning Brothers heard that eight vessels belonging to Canadian National (West Indies) Steamships Ltd. were for sale and so advised Banco. After a survey of the vessels by Flota, Banco decided to purchase them. These vessels, which I understand had been strike-bound for some time, were then lying unmanned at the Port of Halifax and included therein were the seven vessels named as defendants in these proceedings. On August 19, 1958, all parties concerned met at Montreal and Banco purchased all eight vessels. They had been registered in Montreal but the certificates of registration were delivered up and cancelled. On the same date, Banco and Flota signed a Lease-Purchase Agreement covering the eight vessels, as well as others, and the contract—at times referred to as the Canadian contract—is that referred to in the respondent's writ. That document was not before

the Court, but portions of it were referred to in the various affidavits filed. I understand that the contract provided for the operation of all the vessels by Flota and that under its provisions Flota on certain named conditions had an option to purchase them. In August, 1958, Flota took one of the vessels to Baltimore, Maryland, for repairs. The remaining seven vessels remained and still remain at the Port of Halifax unmanned, and, while it was agreed in argument that when owned and operated by the Canadian National (West Indies) Steamships Ltd. they were engaged in commercial pursuits, namely, the carriage of passengers and freight, it was also agreed that they had not been used for any purpose whatever, at least since August 19, 1958, when purchased by Banco.

It will be noted from what I have said that Flota—the plaintiff in the action—is a Cuban corporation and that it asserts no right to ownership or possession of the vessels, its claim being for damages for alleged breach of the contract dated August 19, 1958. It is obvious, therefore, that its purpose in taking proceedings *in rem* and in arresting the defendant vessels was to ensure, if possible, that if successful in its action for damages, the vessels might be available to satisfy any judgment obtained. I should note now that no party, other than the Republic of Cuba, has as yet asserted any rights as owners of or as parties interested in the defendant vessels.

Pottier, D.J.A. rejected the submissions made on behalf of the appellant that the Court was without jurisdiction to hear the matter. While he made no clear finding that the defendant vessels were the property of the Republic of Cuba, it would seem that such was his opinion, for, after considering a large number of cases, he came to the conclusion that the claim of sovereign immunity could not be supported as in his view that principle in regard to ships was applicable only "when ships are involved in matters *jure imperii*", or governmental functions. He was of the opinion after hearing the evidence and after viewing the vessels, that they were equipped for passenger and freight service; that, therefore, their use constituted non-governmental functions, i.e., business matters or *jure gestionis*. He therefore applied the so-called restrictive theory of sovereign immunity and disallowed the appellant's motion. He was

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also of the opinion that the respondent company in the circumstances was not bound to resort to the Courts of Cuba for the determination of its claim for damages, notwithstanding the provisions in the contract.

I propose to consider first the question of sovereign immunity for, if that be determined in favour of the appellant, the remaining question need not be discussed. I find it unnecessary to consider the origin and general principles of this immunity which are discussed in *Dicey's Conflict of Laws*, 7th Ed., p. 129 ff., and in *Cheshire on Private International Law*, 5th Ed., at p. 88 ff.

It is not disputed that the Republic of Cuba is a sovereign state. Its present government, which was in office on August 4, 1960 when these proceedings were instituted, is recognized by Canada and each country has an ambassador in the other country.

The first question that arises is whether the Republic of Cuba is impleaded in these proceedings. The action is *in rem* and while Cuba is not named as a defendant, the writ is directed to "the owners and all others interested in the defendant vessels". As stated in Dicey at p. 135:

> The immunity described protects a foreign State within the meaning of the Rule, in its various manifestations, not only when it is directly sued *in personam*, but also against indirect proceedings.

In the *Cristina*[1], Lord Atkin said:

> In these days it is unusual to name defendants: when the defendants are described as "the owners of a vessel" they can be at once identified. When persons are not entitled the defendants but in the body of the writ are cited to appear as persons claiming an interest, there is said to be some uncertainty whether they appear under leave to intervene or without such leave. In any case when they do appear they appear as defendants, and as such I conceive that they are impleaded. And, when they cannot be heard to protect their interest unless they appear as defendants, I incline to hold that, if they are persons claiming an interest, they are by the very terms of the writ impleaded. But in the present case where persons claiming an interest are the only persons entitled defendants, and the Spanish Government are the only persons claiming an interest adverse to the plaintiffs, I have no doubt not only that the Government were in fact impleaded but were intended by the plaintiffs to be impleaded.

On the basis of the conclusions which I have come to regarding the nature of the appellant's claim to the ownership of and rights of possession and control in the defendant vessels (and which I will now discuss), there can be no

[1] [1938] A.C. 485 at 492.

doubt that in these proceedings the Republic of Cuba was in fact impleaded and was intended by the respondent to be impleaded.

In considering the claim of the appellant, I must keep in mind the statements of Earl Jowitt in the Judicial Committee of the Privy Council in *Juan Ysmael & Co. Inc. v. Indonesian Government*[1], summarized in the headnote as follows:

> A foreign government claiming that its interest in property will be affected by the judgment in an action to which it is not a party and in which it alleges that it is indirectly impleaded, is not bound as a condition of obtaining immunity to prove its title to the interest claimed, but it must produce evidence to satisfy the court that its claim is not merely illusory, nor founded on a title manifestly defective. The court must be satisfied that conflicting rights have to be decided in relation to the foreign government's claim. When the court reaches that point it must decline to decide the rights and must stay the action, but it ought not to stay the action before that point is reached.

The rights of the parties must be determined as of the date of the initiation of these proceedings and the arrest of the ships, namely, August 4, 1960. It is agreed that Banco was the owner of the vessels when it entered into the contract with Flota on August 19, 1958. Whatever rights of possession or control over the defendant vessels that contract conferred on Flota, does not precisely appear, as the contract was not filed. In any event, such rights were clearly abandoned before the end of that year.

In opposing the motion to set aside these proceedings, the respondent filed an affidavit by Lorenzo D. Browning, vice-president and treasurer of Flota, dated November 18, 1960. He stated that following the signing of the Lease-Purchase Agreement with Banco, Flota became the operator of the eight Canadian vessels and that Flota had not consented in any way to the sale of the seven defendant vessels by Banco. An earlier affidavit by Mr. Kerr, counsel for Flota, dated August 4, 1960, and filed in support of the application for the warrant of arrest of the vessels, stated:

> I have been advised by various persons familiar with Cuban affairs and verily believe that it is probable that the said corporation (i.e. Banco) has transferred title to the defendant vessels to some other corporation controlled or operated by the Cuban government.

That affidavit also stated that in view of the uncertainty as to the National character of the vessels and as to their present ownership, it was deemed expedient to serve notice

[1] [1955] A.C. 72.

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of the proceedings upon the Consul General of Cuba at Montreal and on the Cuban Embassy at Ottawa. Such notices, after setting out the nature of the proceedings and the proposed arrest of the ships, state:

> We are sending you a copy of the Writ and Summons. This is to advise you that unless an Appearance in these proceedings is entered within one week exclusive of this date by the owner of the vessels or others interested, the action may proceed to judgment in default.

The appellant's motion was supported by three affidavits of Dr. O. Abello dated August 18, 1960, August 22, 1960 and January 3, 1961. Dr. Abello, then of Havana, Cuba, and a member of the Bar of Cuba, was the legal counselor of the Departmental de Fomento Maritimo "which belongs to the Ministry of Defence of Cuba, which has under its direction all ships and vessels of the Republic of Cuba". Dr. Abello, who joined that department when it was first constituted on February 17, 1959, stated:

> I have personally dealt with all matters relating to the aforementioned steamships and vessels formerly owned by the Canadian National Steamships Ltd. and I have personal knowledge of the facts hereinafter deposed to. In my capacity as counselor to my Department, all legal matters relating to these ships and vessels are under my charge and direction and have been since they were purchased by the Republic of Cuba.

It is clear from the third affidavit of Dr. Abello—and his evidence on this point is not denied—that Flota on or about October 31, 1958, declared that the Canadian contract between Banco and Flota was a nullity in its entirety and that Flota was no longer responsible for any of the vessels. Forming part of that affidavit are copies of two cablegrams sent by Flota to Banco on or about that date, in which it is stated:

> Because of your breach of this contract and your repudiation of the delivery to us by the usurpation of our rights under the contract we have no alternative but to consider we have not accepted those vessels and to consider the Canadian contract a nullity in its entirety. We are therefore hereby tendering delivery to you of the three Rio type vessels and arrangements for delivery can be worked out between your representative and our office in Havana. From the date of this telegram we no longer consider ourselves in any way responsible for any vessels under the Canadian contract which we now consider a nullity . . . As far as the Canadian contract is concerned it is considered a nullity and we must take such action as we deem appropriate.
>
> Following telegram sent to Mr. George Campbell quote you as agent for Banco Cubano Del Comercio Exterior. Requested we turn over to you the keys of Canadian National vessels in Halifax. We are instructing our personnel to turn these keys over to you but we wish you to be on notice as is the bank that your action further substantiates our position that the

bank has repudiated their delivery of these ships to us and we are advising you we in no way consider ourselves responsible for these ships as of yesterday and are cancelling all insurance and other arrangements made by us as of November 3, 1958, with this understanding the keys will be transmitted to you. A copy of this cable is being sent to the bank unquote.

The keys of the vessels were surrendered by Flota and turned over to Banco shortly thereafter. In effect, Flota withdrew entirely from the Canadian contract, declared it a nullity, reserving only the claim for alleged breach of contract. Banco was therefore free to dispose of the vessels as it wished without securing the approval or consent of Flota, and did so on June 9, 1959, by sale to Cuba.

The evidence of Dr. Abello, supported by the exhibits to the affidavits is sufficient at least to satisfy the Court that the appellant's claim to ownership of and right of possession of the defendant vessels is "not illusory nor founded on a title manifestly defective". Indeed, in the absence of any evidence to the contrary (although I recognize that in the particular circumstances of the case it might be difficult for Flota to ascertain the full facts), I would be prepared to find that the appellant has established that Banco did convey all its right, title and interests in the vessels to Cuba on June 9, 1959. Exhibit B, forming part of Dr. Abello's first affidavit, is a photostatic copy of the Agreement of Purchase and Sale of the eight Canadian vessels (*inter alia*) between Banco and Cuba. A translation of the essential parts thereof is attached to the affidavit of A. R. Moreira, dated August 24, 1960. After referring specifically to the eight vessels purchased by Banco from the Canadian National (West Indies) Steamship Company, the following clause appears:

Fourth: That in fulfillment of the offer made by the Cuban Bank of Foreign Commerce and the directions contained in law No. 363 of June 2 of the present year published in the Official Gazette of yesterday he sells, assigns and transfers in the name of his representee and in favour of the Cuban State the shipping and the shipping interests described in the preceding clauses of this instrument with everything belonging and pertaining to them free from encumbrances with all rights and actions inherent in them and without reservations and limitations.

That evidence is supported by the Official Gazette of Cuba, No. 102. It includes Law 363 of the Republic dated June 2, 1959, in which Cuba accepted the offer of Banco to sell all its maritime interests, including the defendant vessels, to Cuba. The evidence also suggests that the right to

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operate the vessels was given to Fomento Maritimo Cubano, an office created on or about February 20, 1959, under the jurisdiction of the Cuban Navy, Ministry of Defence. That office, by Law 600 in October, 1959 was transferred to the Ministry of the Revolutionary Armed Forces, that Ministry being the new name of the Ministry of Defence. Again, in January, 1960, that office was re-organized as a department of the Revolutionary Armed Forces.

Further, the affidavits of Dr. Abello and of J. T. Campbell, accountant of G. T. R. Campbell & Co., Naval Architects, Marine Surveyors and Consultants, of Montreal, show that from June 9, 1959, to August 4, 1960, the vessels were in possession of the Republic of Cuba through its agent, G. T. R. Campbell & Co. Prior to June 9, 1959, that company had supervision of the vessels on behalf of Banco, but on that date Banco and the Republic of Cuba notified them that thereafter the ships were to be supervised on behalf of Cuba as owner thereof. Since that day the Campbell company has supervised the defendant vessels, incurred accounts for dockage and wharfage charges, watching charges, examination of vessels and moorings, etc., on behalf of Cuba, and all accounts therefor have been submitted to that government, represented by either the Officina de Fomento Maritimo (a division of the Department of Defence), or later by the Departmento de Fomento Maritimo (a division of the Ministry of Revolutionary Armed Forces of Cuba).

Some reference should be made to a further document, Exhibit B to Dr. Abello's third affidavit, a translation of which was filed. It is a notarial document dated December 6, 1958, entitled "Minutes of the Delivery of Ships". Flota, represented by its second executive vice-president acting as president, and by its secretary (both residents of Cuba) is said to be a party thereto and I am invited to construe the document as a formal waiver by Flota of all its rights in the vessels referred to in the Canadian contract in favour of Banco, reserving only its claim for damages for breach of the contract. In view of the recitals that the party purporting to act as president of Flota stated that he did not know whether or not he had the power to concur in the Act and that he had done so only at the "requirement" of Banco; and the further recital that the only shareholder of Banco is the Cuban State, I have reached

the conclusion, in view of all the circumstances, that no importance whatever should be given to that document. The evidence is wholly insufficient to satisfy me that it was properly and voluntarily executed by Flota.

I find, therefore, that the seven defendant vessels on August 4, 1960, were the property of the Republic of Cuba and that they were then, and have since remained, in the possession and control of Cuba or of one of its departments, De Fomento Maritimo Cubano, by its Canadian agents, G. T. R. Campbell & Co. It may be noted here that the cost of maintaining and watching the vessels in Halifax Harbour is said to be about $10,000 per month, for all of which Cuba alone has been responsible since June 9, 1959.

On these findings of fact, has the Court jurisdiction to entertain this action—a proceeding in which a Cuban company claims damages for breach of a contract entered into with another Cuban corporation for the operation of the defendant vessels, and when the ownership, possession and control of the vessels has passed from the second corporation to the Republic of Cuba, or at least to one of its departments of state? It is difficult to see how any such claim could succeed if it went to trial since Flota turned over possession of the ships to Banco which had disposed of them by sale before this action was brought. That matter, however, was not one of the grounds on which this motion to set aside the proceedings was based and was not argued before me, and consequently it is unnecessary to consider that matter.

The general rule in regard to the jurisdiction of the Courts when sovereign immunity is claimed is stated in Dicey's *Conflict of Laws,* 1958, 7th Ed., at p. 129, as follows:

> The Court has no jurisdiction to entertain an action or other proceedings against
>
> (1) any foreign State, or the head or government or any department of the government of any foreign State;
>
> (2), (3), (4) Not applicable.
>
> An action or proceeding against the property of any of the foregoing is, for the purpose of this Rule, an action or proceeding against such entity or person.
>
> Provided that the court has jurisdiction to entertain an action or proceeding against any of the foregoing where the defendant therein, duly authorized when necessary, appears, voluntarily waives any privilege and submits to the jurisdiction.

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It will be noted that the Rule as so stated is absolute. Moreover, its application is not limited to ownership of property as shown by the statement in Dicey on pp. 135-6 and the cases there cited.

The immunity described protects a foreign State within the meaning of the Rule, in its various manifestations, not only when it is directly sued *in personam*, but also against indirect proceedings. "[T]he courts . . . will not implead a foreign sovereign. That is they will not by their process make him against his will a party to legal proceedings, whether the proceedings involve process against his person or seek to recover from him specific property or damages. . . . [T]hey will not by their process, whether the sovereign is a party to the proceedings or not, seize or detain property which is his, or of which he is in possession or control." (*The Cristina* [1938] A.C. 485, 490-491, per Lord Atkin) "[T]he rule is not limited to ownership. It applies to cases where what [the foreign State or sovereign] has is a lesser interest, which may be not merely not proprietary but not even possessory." (*The Cristina* [1938] A.C. 485, 507, per Lord Wright) It thus applies where a foreign government has requisitioned a ship without depriving the owners of their possession.

Counsel for the respondent, however, submits that Pottier, D.J.A., was right in applying the restrictive theory of sovereign immunity. That immunity, he says, is available to a foreign state having property in the vessels, if such vessels are engaged in governmental functions, i.e., warships, lightships and the like, but not in cases where the vessels are engaged in non-governmental functions such as the carriage of freight or passengers.

A similar submission was made and rejected in *The Porto Alexandre*[1], a decision of the Court of Appeal in England, the headnote reading as follows:

A vessel owned or requisitioned by a sovereign independent state and earning freight for the state, is not deprived of the privilege, decreed by international comity, of immunity from the process of arrest, by reason of the fact that she is being employed in ordinary trading voyages carrying cargoes for private individuals.

In that case, the *Porto Alexandre* came into the Mersey, got on to the mud, and was salved by three Liverpool tugs. On arresting her to obtain security for the payment of their salvage, the Portuguese Republic put forward a statement that she was a public vessel of the Portuguese Republic, and was therefore exempt from any process in England. Accordingly, the defendants moved to set aside the writ and arrest. The trial Judge granted the application and an appeal therefrom was dismissed, all the members of that Court being of the opinion that they were bound by *The*

[1] [1920] P. 30.

Parlement Belge[1]. The *Porto Alexandre,* formerly a German-owned steamship, by a decision of the Portuguese Prize Court in January, 1917, was adjudged a lawful prize of war. She had been requisitioned by the Portuguese Government and handed over to the Commission of Services of Transports Maritims, and when arrested, was being employed in ordinary trading voyages earning freight for the Government.

In that case, Warrington, L. J. said at p. 36:

> Whatever may be the actual use to which this ship is put, I think the evidence is quite sufficient to show that it is the property of the State, and is destined to public use; and, that being so, the case seems to me to come exactly within the principle of the judgment in *The Parlement Belge* with the result which I indicated at the beginning of my judgment.

Scrutton, J. quoted with approval the statement in the 7th Ed., Hall's *International Law,* p. 211, where, after dealing with warships and public vessels so-called, the author stated:

> If, in a question with respect to property coming before the courts a foreign state shows the property to be its own, and claims delivery, jurisdiction at once fails, except insofar as it may be needed for the protection of the foreign state.

Both the above cases were considered in *Compania Naviera Vascongado v. S.S. Cristina*[2], a unanimous decision of the House of Lords affirming a decision of the Court of Appeal, affirming the decision of Bucknill, J. The headnote reads as follows:

> A ship, called the *Cristina,* belonging to the appellants, a Spanish company, and registered at the port of Bilbao, was lying in the port of Cardiff. Shortly before her arrival there, but after she had left Spain, a decree was made by the Spanish Government requisitioning all vessels registered at the port of Bilbao, and in view of this, and acting on the instructions of the Spanish Government, the Spanish consul at Cardiff went on board the *Cristina,* stated that she had been requisitioned, dismissed the master and put a new master in charge. Thereupon the appellants issued a writ in rem claiming possession of the *Cristina* as their property. The Spanish Government entered a conditional appearance, and gave notice of motion for an order that the writ should be set aside inasmuch as it impleaded a foreign sovereign State:
>
> *Held,* that the Courts of this country will not allow the arrest of a ship, including a trading ship, which is in the possession of, and which has been requisitioned for public purposes by, a foreign sovereign State, inasmuch as to do so would be an infraction of the rule well established in international law that a sovereign State cannot, directly or indirectly, be

[1] (1880) 5 P.D. 197. [2] [1938] A.C. 485.

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impleaded without its consent, and, therefore, that the writ and all subsequent proceedings must be set aside: *The Broadmayne* [1916] P. 64; *The Messicano* (1916) 32 Times L.R. 519; *The Crimdon* (1918) 35 Times L.R. 81; *The Gagara* [1919] P. 95; and *The Jupiter* [1924] P. 236 approved and applied.

The first judgment was given by Lord Atkin who said at p. 490:

> The foundation for the application to set aside the writ and arrest of the ship is to be found in two propositions of international law engrafted into our domestic law which seem to me to be well established and to be beyond dispute. The first is that the courts of a country will not implead a foreign sovereign, that is, they will not by their process make him against his will a party to legal proceedings whether the proceedings involve process against his person or seek to recover from him specific property or damages.
>
> The second is that they will not by their process, whether the sovereign is a party to the proceedings or not, seize or detain property which is his or of which he is in possession or control. There has been some difference in the practice of nations as to possible limitations of this second principle as to whether it extends to property only used for the commercial purposes of the sovereign or to personal private property. In this country it is in my opinion well settled that it applies to both.

Lord Wright seems to have been of the same opinion. At p. 512, after referring to *The Porto Alexandre* and to *The Parlement Belge*, as well as to other English and United States decisions, he said:

> This modern development of the immunity of public ships has not escaped severe, and, in my opinion, justifiable criticism on practical grounds of policy, at least as applied in times of peace. The result that follows is that Governments may use vessels for trading purposes, in competition with private ship-owners, and escape liability for damage, and salvage claims. Various international conventions have discussed this problem and have culminated in the International Convention for the Unification of Certain Rules concerning the Immunity of State-owned ships, of April 10, 1926. The general purport of the Convention was to provide that ships owned or operated by States were to be subject to the same rules of liability as privately owned vessels; ships of war, State-owned yachts, and various other vessels owned or operated by a State on Government and non-commercial service were excepted. There was power for a State to suspend the operation of the Convention in time of war. Great Britain, along with the majority of modern States, signed the Convention, but has not yet ratified it or enacted any legislation to bring it into effect in this country. But even if the provisions of the Convention were made law here, it is not clear that it would affect the position in the present case, because its effect is apparently limited to claims in respect of the operation of such ships or in respect of the carriage of cargoes in them. Thus it would affect claims in rem for collision damage such as the claim in *The Parlement Belge*, 5 P.D. 197 or for salvage as in *The Broadmayne*, [1916] P. 64 and *The Porto Alexandre*, [1920] P. 30 or for cargo damage as in *The Pesaro*, 271 U.S. 562, but it may be, not claims for possession such as that in the present case or *The Gagara* [1919] P. 95 or *The Jupiter*, [1924] P. 236.

I may add that in the present case it is in my opinion sufficiently shown by the evidence before the Court that the Spanish Government had actually requisitioned, and taken possession and control of, the *Cristina*. That is all that is needed to justify the claim to immunity on the ground of "property." The question how far a mere claim or assertion by that Government would be conclusive on the Court, does not arise here.

And, at pp. 504-5, Lord Wright said:

To take the present case the writ names as defendants the *Cristina* and all persons claiming an interest therein, and claims possession. The writ commands an appearance to be entered by the defendants (presumably other than the vessel) and gives notice that in default of so doing the plaintiffs may proceed and judgment be given by default, adjudging possession to the plaintiffs. A judgment in rem is a judgment against all the world, and if given in favour of the plaintiffs would conclusively oust the defendants from the possession which on the facts I have stated they beyond question de facto enjoy. The writ by its express terms commands the defendants to appear or let judgment go by default. They are given the clear alternative of either submitting to the jurisdiction or losing possession. In the words of Brett L.J. the independent sovereign is thus called upon to sacrifice either its property or its independence. It is, I think, clear that no such writ can be upheld against the sovereign State unless it consents.

Lord Thankerton, while agreeing that the *Cristina* was dedicated to public uses—as in *The Parlement Belge* case—expressed doubts that sovereign immunity applied to ships "being used in ordinary commerce" as in the *Porto Alexandre,* but expressed no final opinion on the matter, reserving the right to re-consider the decision in that case. Lord Macmillan also reserved his opinion on this point. At p. 498, he said:

I confess that I should hesitate to lay down that it is part of the law of England that an ordinary foreign trading vessel is immune from civil process within this realm by reason merely of the fact that it is owned by a foreign State, for such a principle must be an importation from international law and there is no proved consensus of International opinion or practice to this effect. On the contrary the subject is one on which divergent views exist and have been expressed among the nations. When the doctrine of the immunity of the person and property of foreign sovereigns from the jurisdiction of the Courts of this country was first formulated and accepted it was a concession to the dignity, equality and independence of foreign sovereigns which the comity of nations enjoined. It is only in modern times that sovereign States have so far condescended to lay aside their dignity as to enter the competitive markets of commerce, and it is easy to see that different views may be taken as to whether an immunity conceded in one set of circumstances should to the same extent be enjoyed in totally different circumstances.

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Lord Maugham, while agreeing in the result because of the special circumstances of the case, expressed his opinion that the principle of sovereign immunity should not be applied to State-owned ships engaged in commerce. At p. 522 he said:

> My Lords, I am far from relying merely on my own opinion as to the absurdity of the position which our Courts are in if they must continue to disclaim jurisdiction in relation to commercial ships owned by foreign Governments. The matter has been considered over and over again of late years by foreign jurists, by English lawyers, and by business men, and with practical unanimity they are of opinion that, if Governments or corporations formed by them choose to navigate and trade as ship-owners, they ought to submit to the same legal remedies and actions as any other shipowner. This was the effect of the various resolutions of the Conference of London of 1922, of the Conference of Gothenburg of 1923 and of the Genoa Conference of 1925. Three Conferences not being deemed sufficient, there was yet another in Brussels in the year 1926. It was attended by Great Britain, France, Germany, Italy, Spain, Holland, Belgium, Poland, Japan and a number of other countries. The United States explained their absence by the statement that they had already given effect to the wish for uniformity in the laws relating to State-owned ships by the Public Vessels Act, 1925 (1925, c. 428). The Brussels Conference was unanimously in favour of the view that in times of peace there should be no immunity as regards State-owned ships engaged in commerce; and the resolution was ratified by Germany, Italy, Holland, Belgium, Esthonia, Poland, Brazil and other countries, but not so far by Great Britain. (Oppenheim, International Law, 5th ed., vol. I, p. 679.)

The opinion of Lord Atkin in the *Cristina*, that the rule of sovereign immunity extends to property of a foreign sovereign or state even if that property be used for commercial purposes, has been commented on with approval in a number of texts in recent years. I have already stated the rule as found in Dicey at p. 129. At p. 132 the author states:

> In the second place, the English courts accord full immunity from suit to foreign States, etc., without regard to the nature of the activity out of which the cause of action arises. No distinction is made, in particular, between the personal activities of heads of foreign States and their official acts.
>
> Nor is any line drawn between public law activities and private law activities, nor between acts pertaining to sovereign functions, and commercial transactions. A line of the latter sort, though it is clearly very difficult to draw, is, however, discernible in the practice of at least some other States and it may well be that the system of international law as a whole is moving towards a "functional" concept of jurisdictional immunities which would confine their scope to matters within the field of activity conceived as belonging essentially to a person of that system of whatsoever category.

In Marsden's *Collisions at Sea*, 1953, 10th Ed., the author says at p. 236:

The courts of this country have no jurisdiction to entertain any action or other proceeding against a foreign sovereign or sovereign State, subject to the proviso that appearance, waiver of privilege and submission to the jurisdiction may be voluntarily made, in which case the court has jurisdiction in the cause but no power to enforce any decree by execution in any form. Immunity extends to ambassadors and diplomatic agents duly accredited, members of their suites, and persons and organizations protected by the Diplomatic Privileges Act, 1708, the Diplomatic Privileges (Extension) Acts of 1941, 1944 and 1946, or the Diplomatic Immunities (Commonwealth Countries and Republic of Ireland) Act, 1952, subject to the same proviso. Proceedings *in rem* cannot be taken against the public ship of a foreign sovereign.

In Oppenheim's *International Law*, 8th Ed., 1955, p. 856, the author says:

451*a*. The increasing practice of Governments of owning or controlling merchant-ships, either for purposes connected with public services such as the carriage of the mails or the management of railways, or simply for the purpose of trade, has led to some doubts as to whether they are entitled to the immunities which are enjoyed by men-of-war. The practice of the courts of different States in this matter is far from being uniform. In Great Britain the practice is still probably as follows. As the result of a series of decisions, of which *The Parlement Belge* (a Belgian public mail-ship) in 1880 may fairly be regarded as the starting-point of the movement in favour of immunity: (*a*) a British court of law will not exercise jurisdiction over a ship *which is the property of a foreign State*, whether she is actually engaged in the public service or is being used in the ordinary way of a shipowner's business, as, for instance, being let out under a charter-party; nor can any maritime lien attach, even in suspense, to such a ship so as to be enforceable against it if and when it is transferred to private ownership.

In Cheshire on *Private International Law*, 5th Ed., 1957, the author states at p. 90:

On the principle that sovereign States are equal and independent the rule has come to be that no sovereign independent State will exercise any jurisdiction over the person or the property of any other sovereign State.

Then, after stating that the law has been reduced to two principles by Lord Atkin in *The Cristina* (*supra*) and after referring to *The Parlement Belge*, he continues at p. 91:

It can, at any rate, be affirmed that in the following cases the immunity is unlimited.

First, where the sovereign State is the admitted owner of the subject-matter of the suit, as in the case of a warship or of the cross-channel steamer in *The Parlement Belge*.

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In the present case, while the respondent does not admit that the appellant is the owner of the defendant vessels, the evidence is sufficient to satisfy me that Cuba is, in fact, the owner.

While the matter is perhaps not entirely free from doubt, I have come to the conclusion that I should follow the rule as laid down by Lord Atkin in *The Cristina* and which has been cited with approval by the well-known textbook writer to whom I have referred. It was also followed in a Canadian case, that of *Thomas White v.* The Ship *Frank Dale*[1], by Sir Joseph Chisholm, D.D.J.A. Reference may also be made to the opinion of Duff, C.J.C. in *Reference as to Power to Levy Rates on Foreign Legations and High Commissioners' Residences*[2]; and to the judgment of Locke J. in *Municipality of Saint John et al. v. Fraser-Bruce Overseas Corp. et al.*[3].

It is to be noted, also, that the reservations of Lord Thankerton, Lord Macmillan and Lord Maugham in *The Cristina* appear to be limited to ships engaged in ordinary commerce or trading. If that be so, it would seem that in general they were inclined to adopt the principles set forth in The International Convention for the Unification of Certain Rules Concerning the Immunity of State-Owned Ships of April 10, 1926 (Brussels Convention). But, as stated by Lord Wright in that case, the Convention was not ratified by Great Britain; then he stated also at pp. 512-13:

> Great Britain, along with the majority of modern States, signed the Convention, but has not yet ratified it or enacted any legislation to bring it into effect in this country. But even if the provisions of the Convention were made law here, it is not clear that it would affect the position in the present case, because its effect is apparently limited to claims in respect of the operation of such ships or in respect of the carriage of cargoes in them. Thus it would affect claims in rem for collision damage such as the claim in *The Parlement Belge*, 5 P.D. 297, or for salvage as in *The Broadmayne* [1916] P. 64, and *The Porto Alexandre*, [1920] P. 30, or for cargo damage as in *The Pesaro*, 271 U.S. 562, but it may be, not claims for possession such as that in the present case or *The Gagara*, [1919] P. 95, or *The Jupiter*, [1924] P. 236.

I have examined the text of that Convention and it would seem to me also that its effect is limited to claims in respect of the operation of such ships or in respect of the carriage of goods in them.

[1] [1946] Ex C.R. 555. [2] [1943] S.C.R. 208 at 229-30.
[3] [1958] S.C.R. 263 at 280-1.

In the instant case, the respondent's claim does not arise from the operation of the defendant vessels but rather from a contract respecting the operation of the vessel. The fact is that while the vessels were originally equipped and used for the carriage of freight and passengers, they had been put to no commercial purposes since about 1956 or 1957 and have never been used for commercial or any other purposes by either Banco or Cuba. They were strike-bound at first and since the purchase by Banco have remained idle at the Port of Halifax. Moreover, there is no evidence that the Republic of Cuba intended to use them for commercial purposes. It is shown that Cuba made an unsuccessful effort to sell them through a New York broker and that Dr. Abello came to Canada in August, 1960 as representative of Cuba to have them taken to Cuba, but for what purposes is not known.

For the reasons stated and having come to the conclusion that the claim of the Republic of Cuba to ownership of the vessels is well founded and not illusory nor founded on a title manifestly defective; and that conflicting rights have to be decided in relation to the claim of the Republic of Cuba, I must decline to decide the rights and stay the action—to use the language of Earl Jowitt in *The Juan Ysmael & Co.* case (*supra*).

Accordingly, the appeal will be allowed, the writ and warrants of arrest in this action and service thereof will be set aside as the Court is without jurisdiction to entertain the action. The appellant is entitled to be paid its costs both in this Court and in the Court below, after taxation.

Before leaving the matter, however, I must refer to certain oral evidence given on April 7, 1961, by Dr. Abello on behalf of Flota. In his judgment, the learned District Judge in Admiralty ruled that such evidence was inadmissible and at the hearing of the appeal counsel for Flota asked that that ruling be reversed.

That evidence was tendered under rather unusual circumstances. It seems that prior to that date, counsel for both parties had completed their submissions and the matter was standing for judgment. On that date, counsel for Flota again appeared before the District Judge and asked for leave to present further oral evidence by Dr. Abello who at that time had left Cuba, being wholly

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dissatisfied with conditions under the present regime in that country. Mr. McInnes, counsel for the appellant, on that date had written to the District Judge as follows:

> Our retainer with respect to the aforementioned litigation has been terminated and, consequently, I wish to advise you that we are no longer acting in the matter. It may be that the Cuban Government wish to retain other solicitors in Halifax to act on their behalf. My purpose in writing to you is to advise you of the fact that on instruction we are retiring from this case.

Counsel for Flota, after referring to that letter, then stated:

> The situation is extremely complicated in that Dr. Oscar Abello, originally retained Mr. McInnes and his firm, and Dr. Abello has been in touch with Mr. McInnes recently and the result of that conference is the letter Your Lordship has received, that Mr. McInnes is no longer retained. Dr. Abello indicated to Mr. McInnes, I understand, that he would like to discuss this case with Mr. Black and myself and I was contacted by Mr. Dickey last night who advised me it was entirely proper for Dr. Abello to see us and discuss the case with us. As a result of what Dr. Abello has told us, we have decided to come to your Lordship to ask to hear the evidence of Dr. Abello as it relates to the problem of sovereign immunity and the ownership of the vessels.
>
> The Court faces one difficult problem, and that is that there is no one here representing the Defendant vessels.

Certain evidence was then given by Dr. Abello, not only on the question of sovereign immunity and the ownership of the vessels, but also as to the nature of the Courts as they are now constituted in Cuba. I have no doubt that counsel for Flota acted in good faith throughout and with the sole desire of assisting the Court by the production of all available evidence. I think, however, that Pottier, J. was right in rejecting that evidence. In his judgment, he said at p. 23:

> There was evidence given on April 7 by Dr. Oscar Abello, and an objection was made against the reception of this evidence or the consideration of it as a part of the application herein. I was asked to make a ruling regarding the same. I find that it was given after the close of all representations by way of evidence and do not consider it a part of this application.

It seems to me that as the matter was standing for judgment prior to April 7, 1961, no further evidence should have been received without proper notice to the claimant—the Republic of Cuba; and that as Mr. McInnes' retainer had been then withdrawn, the application to hear further evidence by Dr. Abello should have been adjourned to enable the claimant to secure other counsel if so advised. I may

add that counsel for Flota intended on the hearing of this appeal to ask leave to adduce evidence by Dr. Abello, but unfortunately he was in the United States and had refused to attend.

Judgment accordingly.

BETWEEN:

1960
Nov. 28
1961
June 19

BENOIT GONTHIER .....SUPPLIANT;

AND

HER MAJESTY THE QUEEN .....RESPONDENT.

Crown—Costs—Advocate appointed legal agent by Department of Justice subject to agreement his bill would be taxed by Deputy Minister whose taxation was not appealable—Whether agreement binding—Whether appeal lies to Exchequer Court—The Bar Act, S. of Q., 1953-54, c. 59 as amended—Bar of the Province of Quebec, by-laws 66, 67—Civil Code of Quebec, arts. 990, 1732—Exchequer Court Act, R.S.C. 1952, c. 98, s. 36(1).

Suppliant, a Montreal advocate, was engaged as legal agent by the Department of Justice and supplied with a document entitled "Instructions to Agents" which specified that an agent in submitting his account was to certify that the services indicated therein truly showed their nature, the time occupied, and the fees claimed. It further provided that such account was taxable by the Deputy Minister of Justice whose taxation was not appealable.

Acting on the Department's instructions suppliant laid complaints against and prosecuted two persons for offences under the *Excise Act*. The accused pleaded guilty in the Court of Sessions of the Peace and were each fined $1,000 and costs. On an appeal the fines were reduced to $500 each and costs. Subsequently suppliant laid similar charges against 122 others all of whom pleaded guilty and were each fined $1,000 and costs. Suppliant then submitted two accounts to the Department, one for $130 covering his fees for the first two convictions secured, and a second for $1,360, his fees for the subsequent convictions. The first account was taxed at the amount submitted and the second at $380. Suppliant by Petition of Right sought to secure from the respondent the difference between the amount of his bill and that paid him. He alleged that he had complied with the terms of the "Instructions to Agents" and that the fees claimed by him were in accordance with its provisions. In the alternative he alleged that the instructions were *ultra vires* and that his fees were governed by the provisions of the *Bar Act*, S. of Q. 1953-54, c. 59 as amended, and by-laws 66 and 67 of the Federal Council of the Quebec Bar.

Held: That there was nothing in the provisions contained in the "Instructions to Agents" which if followed would lead the suppliant open to a charge of having committed an act derogatory to his profession.

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Although the profession of advocates is governed by the *Bar Act*, advocates as agents, are by virtue of art. 1732 of the *Civil Code* subject, insofar as they apply, to the general rules governing mandates, and it could not be argued that the contract of agency in question contravened art 990 of the *Code* which states that the consideration is unlawful when it is prohibited by law or is contrary to good morals or public order.

2. That the suppliant was bound by the contract of agency by which the Deputy Minister of Justice was given wide discretionary powers to determine the amount of his account and, in the absence of evidence to justify the conclusion that the taxing officer had acted in bad faith, or that the amount at which the account was taxed was unreasonable, there was no reason that the Court should interfere.
3. That although the "Instructions to Agents" specified the taxation was not appealable, s. 36(1) of the *Exchequer Court Act* vested jurisdiction in the Court to hear an appeal therefrom.

PETITION OF RIGHT by a member of the bar to recover professional fees.

The action was tried before the Honourable Mr. Justice Kearney at Ottawa.

Benoit Gonthier on his own behalf.

Paul M. Ollivier for respondent.

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

KEARNEY J. now (June 19, 1961) delivered the following judgment.

Dans cette affaire, un membre du barreau de Montréal réclame de la Couronne, par voie de pétition de droit, $1,490 pour honoraires professionnels.

Les faits ne sont pas contestés. Par lettre du 4 octobre 1957 (pièce A), avec directives aux corrrespondants (p. 1) y incluses, le sous-ministre de la Justice nommait le pétitionnaire correspondant légal ou agent. Ces directives mettent au point les devoirs et responsabilités de l'agent ainsi que les honoraires accordés pour ses services.

Au cours du mois de décembre 1959, le Ministère du Revenu National a demandé au pétitionnaire de représenter la Couronne et de porter plainte contre Anna-Maria De Castris et Cesina Vitoline, de la cité et du district de Montréal, pour infraction à l'article 163 de la *Loi de l'Accise*, S.R.C. 1952, c. 99, dont les prescriptions pertinentes prévoient que—

163(1) Quiconque, qu'il en soit ou non propriétaire, vend ou offre en vente, ou achète, ou a en sa possession de l'eau-de-vie illégalement fabriquée ou importée, ou de l'eau-de-vie illégalement ou frauduleusement

enlevée de toute distillerie, manufacture-entrepôt ou de tout entrepôt en douane, sans excuse valable, dont la preuve incombe à l'accusé, est coupable d'un acte criminel, et doit être condamné

a) pour une première infraction,

(i) à une amende d'au plus deux mille dollars et d'au moins cent dollars,

(ii) à un emprisonnement, avec ou sans travaux forcés, pour une période d'au plus douze mois et d'au moins trois mois, ou

(iii) à l'amende et l'emprisonnement à la fois, et, faute de paiement d'une peine pécuniaire prévue par le sous-alinéa (i) ou (iii), à un emprisonnement d'au plus douze mois et d'au moins trois mois en sus de l'emprisonnement, s'il en est, imposé aux termes du sous-alinéa (ii) ou (iii); . . . .

Le pétitionnaire soutient qu'en conformité des directives reçues de la part du Ministère de la Justice, il a dûment rempli son mandat. Il ajoute que les deux accusées ont été assignées et ont comparu devant la Cour des Sessions de la Paix du District de Montréal; qu'elles ont plaidé coupables auxdites plaintes. Le 19 février elles furent condamnées à une amende de $1,000 et les frais ou, à défaut de paiement, à trois mois d'emprisonnement. Un appel fut interjeté, basé sur la sévérité de la sentence, laquelle, le 21 avril 1960, fut réduite à $500 d'amende et les frais, ou à trois mois d'emprisonnement.

Par suite des perquisitions effectuées par la Royale Gendarmerie dans les causes susmentionnées, le pétitionnaire, sur la demande du sous-ministre, poursuivit en justice 122 autres accusés soupçonnés d'infractions semblables qui, à leur comparution, ont tous plaidé coupables et furent condamnés à payer une amende de $1,000 et les frais. La réclamation du pétitionnaire, comme on le verra plus loin, ne porte que sur les services rendus à l'égard de ces 122 poursuites.

Le ou vers le 23 février 1960, le pétitionnaire se rendit au cabinet du directeur intérimaire, division du droit criminel, Ministère de la Justice, à Ottawa, pour y présenter son compte, préparé, dit-il, en conformité des directives qu'il avait reçues et selon sa manière de les interpréter. Le directeur interpréta les directives autrement, en insistant sur le fait que le pétitionnaire aurait dû calculer ses honoraires d'après le nombre d'heures consacrées à la tâche.

Le 15 mars 1960 le pétitionnaire envoya deux comptes au sous-ministre de la Justice: un de $130 pour honoraires dans les causes de Des Catris et Vitrolini, lequel n'a pas été

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déposé; et l'autre de $1,360 pour ses honoraires touchant les 122 plaintes subséquentes, lequel a été déposé comme pièce justificative 2. Par suite de l'envoi des deux comptes susmentionnés, un malentendu se serait produit attribuable, à mon avis, aux faits suivants: Quelque temps après réception des deux comptes, le directeur intérimaire de la division du droit criminel taxa le premier à $130 et le second à $380, puis il les expédia pour acquittement à la division de la Douane et de l'Accise du Ministère du Revenu National. Peu de temps après, un autre directeur intérimaire avisa le pétitionnaire, soit le 7 avril, d'adresser toute autre communication au sujet de son compte au ministre du Revenu National. Le pétitionnaire considéra cette lettre comme un refus de paiement de la part du Ministère de la Justice et, n'ayant reçu rien d'autre, enregistra la présente requête le 2 mai 1960; le 6 mai il reçut du Ministère du Revenu National une lettre portant la date du 3 mai 1960 (p. 3) avec chèque y inclus de $510, dont $130 pour ce compte tel que présenté, et $380 à titre d'acquittement du second compte de $1,360. Le 6 mai le pétitionnaire encaissa ledit chèque sous toutes réserves. Il est donc clair que le seul montant en litige est celui de $1,360.

Tel qu'il appert au premier article de la pièce justificative 2, le pétitionnaire a exigé $610 pour travail accompli hors de cour en la préparation de 122 plaintes et mandats de comparution, à $5 chacun. Le pétitionnaire n'a apporté aucune preuve des heures qu'il y avait consacrées; et le préposé à la taxation a accordé $5 pour la préparation de la première plainte et cinq heures à $10 l'heure pour la préparation du reste, soit cent vingt et une plaintes qui, du reste, étaient substantiellement semblables à la première, les noms et les dates exceptés, se chiffrant à $55; et une somme supplémentaire de $40 pour la vérification et la transcription des plaintes, faisant un total de $95.

Le solde du compte, soit $750, se rapportait aux dix-neuf heures en cour lorsque les accusés comparaissaient en groupes et, individuellement, s'avouaient coupables.

La répartition du montant démontre que le pétitionnaire a chargé $5 pour le premier accusé d'un groupe qui plaidait coupable, et $5 pour chacun des autres du même groupe qui plaidait de la même manière. Le service de taxation du

Ministère de la Justice a accordé au pétitionnaire $15 l'heure pour vacation à la cour, notamment $285, et taxa donc le compte en entier à $380.

Le pétitionnaire soutient qu'il s'est en tout conformé aux termes et conditions des directives aux agents tels que prévus à la pièce 1; que les honoraires qu'il réclame sont conformes aux prescriptions de l'annexe A de ladite pièce et, alternativement, que ces directives sont *ultra vires;* et que les honoraires qui lui sont dus sont régis par les prescriptions de la *Loi du Barreau* de la province de Québec, 2-3 Eliz. II, ch. 59, art. 9, modifiée par 3-4 Eliz. II, ch. 41, et les règlements 66 et 67 mis en vigueur par le conseil général du barreau, dont les prescriptions pertinentes prévoient que—

9. Les avocats en exercice ont seuls droit à des honoraires judiciaires et extrajudiciaires.

Le conseil général du barreau de la province peut faire, modifier et remplacer des tarifs d'honoraires judiciaires pour les avocats exerçant devant les tribunaux de la province. Toutefois, ces tarifs n'entrent en vigueur que sur l'approbation du lieutenant-gouverneur en conseil.

* * *

Le conseil général peut arrêter, modifier et remplacer des tarifs d'honoraires extrajudiciaires. Ces tarifs entrent en vigueur à la date fixée par le conseil général.

66. Se rend coupable d'un acte dérogatoire à l'honneur et à la dignité de la profession l'avocat qui pose, entre autres, les actes suivants:

Suit une longue énumération d'actes que j'estime inapplicables aux faits de la présente cause.

67. En vue de prévenir, concilier ou pacifier les différends qui peuvent surgir entre un avocat et son client, concernant la valeur de services rendus par un membre du Barreau, le conseil de section, sur demande présentée au syndic par le client, peut ordonner une enquête par trois avocats nommés par le conseil.

Pour disposer tout de suite de ce dernier point, je ne vois rien dans les relations entre les parties en cause qui, aux termes de la pièce 1, rendrait le pétitionnaire coupable d'un acte dérogatoire à l'honneur et à la dignité de sa profession. La profession d'avocat est réglée par la *Loi du Barreau,* mais à titre d'agents les avocats, aux termes de l'article 1732 du *Code Civil,* dont ci-dessous le texte, sont sujets aux règles

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générales qui régissent les contrats, y compris les mandats, dont il est question au titre VIII du *Code Civil*, en autant que ces règles sont applicables:

Art. 1732. Les avocats, les procureurs et les notaires sont sujets aux règles générales contenues dans ce titre, en autant qu'elles peuvent s'appliquer. La profession d'avocat et procureur est réglée par les dispositions contenues dans l'acte intitulé: *Acte concernant le Barreau du Bas Canada*, et celle des notaires par un acte intitulé: *Acte concernant le Notariat.*

On ne peut se plaindre à juste titre que le mandat en question enfreint l'article 990 C.C., ci-dessous cité:

Art. 990. La considération est illégale quand elle est prohibée par la loi, ou contraire aux bonnes mœurs ou à l'ordre public.

En regard de la somme de $610 réclamée pour la rédaction des plaintes et sommations, il n'y a absolument rien dans le compte du pétitionnaire quant aux heures consacrées à ce travail et il n'a fourni aucune preuve à l'appui de ce montant; pour le justifier, il comptait entièrement sur l'annexe A, alinéa *c*), qui suit:

Rédaction de la plainte et de la sommation (en tout) $5.00
Si la plainte comporte plus d'un chef d'accusation contre une même personne, l'honoraire additionnel pour chaque chef sera de 3.00

Premièrement, le procureur de la Couronne a signalé à la cour que le pétitionnaire a négligé de se conformer au paragraphe 15 *b*), ci-dessous cité, des directives, où l'on peut constater l'importance des précisions sur le temps employé:

Il faut mentionner *le temps* qu'on a véritablement consacré aux conférences, entrevues ou autres vacations, par exemple à un procès ou à l'audition d'un appel, pour lesquelles on réclame des honoraires.

Deuxièmement, vu qu'il ne s'agit pas ici d'une plainte portée en vertu d'un article du *Code Criminel*, S.R.C. 1927, c. 146, art. 1, mais de poursuites multiples sous la *Loi de l'Accise*, art. 163, il faut, en le lisant avec l'alinéa *c*) ci-dessus, faire valoir l'alinéa *q*) de l'annexe A qui se lit ainsi:

Nonobstant ce que prévu aux paragraphes de cette annexe, les honoraires accordés dans les cas de poursuites multiples, sous toute autre loi, ne devront pas excéder une somme raisonnable basée sur le temps y consacré tant pour la préparation qu'en cour.

Or, au titre «Interprétation» du Code Criminel, l'article 2(45) [2(1) dans le code rédigé en anglais] décrète que—

«toute loi», «une loi» ou «toute autre loi» comprend toute loi adoptée ou qui doit l'être par le Parlement du Canada, ...

Donc, il est évident que la *Loi de l'Accise* susmentionnée est une «autre loi» au sens où l'entend l'article précité du Code Criminel.

Comme je l'ai déjà signalé, l'avocat de l'intimée a déclaré que le Ministère de la Justice estimait cinq heures suffisantes à la rédaction desdites plaintes et sommations, toutes du même genre. Citons à ce sujet l'alinéa *d*) de l'annexe A:

> A chaque item concernant la préparation du procès ou une entrevue ou conférence avec des policiers, fonctionnaires d'un ministère, magistrats, témoins ou autres personnes ou une vacation à la cour, il faut mentionner le temps qu'on y a véritablement consacré chaque jour. Honoraires, par heure $10.00

L'intimée a donc accordé $10 l'heure pour la rédaction en question et $40 pour transcription et vérification, $5 supplémentaires pour la première plainte, en tout $95. A mon sens, le pétitionnaire n'a pas prouvé qu'aux termes de l'annexe A il avait droit à plus de $95 en regard de cet item.

Quant au solde de sa réclamation, soit $750, le pétitionnaire s'appuie en partie sur l'alinéa *f*) de l'annexe A, que voici:

> Si l'accusé plaide «coupable» l'honoraire d'audition sera de .....$15.

L'annexe A ne comporte aucune disposition visant précisément une situation comparable à celle faisant l'objet de la présente cause, où comparaissent à la fois plusieurs accusés qui s'avouent coupables les uns après les autres sans perte de temps. Le pétitionnaire ne réclame pas $15 pour chaque accusé plaidant coupable, mais advenant une telle réclamation la somme de $750 serait de $1,830. Il a exigé $15 pour le premier accusé de chaque groupe plaidant coupable et $5 chacun pour les autres agissant ainsi. En ce faisant, le pétitionnaire aurait, je crois, appliqué par analogie l'alinéa *g*) cité ci-dessous:

> Si l'accusé plaide «coupable» à plus d'un chef d'accusation l'honoraire pour chaque chef additionnel sera de ..... $5.00.

L'avocat de la Couronne a prétendu, et je crois que c'est à juste titre, que l'alinéa *f*) sur lequel est fondée la réclamation de $750, doit, de la même façon que l'alinéa *c*) lorsqu'il s'est agi de la réclamation de $610, être lu conjointement avec l'alinéa *q*) de l'annexe A, et que, par conséquent, pour les dix-neuf heures de vacations à la cour, au cours

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desquelles tous les accusés ont plaidé coupables, le pétitionnaire avait droit à $15 pour chacune de ces heures, ou $285 en tout.

Le pétitionnaire fit entendre un autre argument visant à la justification des honoraires exigés, notamment, que le sous-ministre de la Justice n'avait pas le droit de taxer son compte, parce qu'il avait été engagé par la division de la Douane et de l'Accise, et il cita à l'appui le paragraphe 12 de la pièce justificative 1, que voici:

> Si le correspondant a reçu ses instructions d'un autre ministère que le nôtre, il doit soumettre son compte directement à ce ministère-là.

Le pétitionnaire avait reçu ses directives du Ministère de la Justice bien avant d'avoir été autorisé par la division de la Douane et de l'Accise à représenter le ministre de la Justice; et le fait qu'il agissait en qualité de correspondant du Ministère de la Justice est irréfutablement établi par le certificat signé de sa main, en conformité du paragraphe 14 des Directives aux Correspondants (voir la dernière page de la pièce 2), qui se lit ainsi:

> Ils doivent certifier tous les exemplaires de leur compte dans les termes qui suivent:
>
> JE CERTIFIE AVOIR RENDU LES SERVICES DÉCRITS DANS CE COMPTE ET QUE CELUI-CI INDIQUE FIDÈLEMENT LEUR NATURE ET LEUR DURÉE, AINSI QUE LES HONORAIRES RÉCLAMÉS, LES DÉBOURSÉS ENCOURUS ET TOUTES LES SOMMES D'ARGENT REÇUES PAR MOI DANS CETTE AFFAIRE.
>
> (Signé) Benoît Gonthier,
> Correspondant du Ministère de la Justice.

Les parties ont discuté brièvement le paragraphe 13 sousmentionné des directives, qui à mon avis mérite une attention particulière:

> Les comptes des correspondants pour services professionnels sont taxés par le sous-ministre de la Justice, dont la décision est sans appel. C'est là une condition de tout mandat qui leur est confié.

Nonobstant ce dernier paragraphe cité, je n'ai aucun doute que le pétitionnaire a un droit d'appel de la taxation pratiquée, qui fait l'objet de la présente cause, et qu'il est du ressort de cette cour de l'entendre en vertu des dispositions très générales de l'article 36(1) de la *Loi sur la Cour de l'Echiquier*, S.R.C. 1952, c. 98, qui décrète que

> Toute réclamation contre la Couronne peut être poursuivie par pétition de droit, ou peut être déférée à la Cour par le chef du ministère dont l'administration a occasionné la réclamation.

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Je ne veux pas que ce que je vais dire soit compris comme signifiant que, si j'avais été à la place du préposé à la taxation, je n'aurais pas augmenté quelque peu le montant qu'il a accordé au pétitionnaire, mais je dois dire que ledit pétitionnaire n'a pas présenté de preuve touchant la valeur des services rendus et le rang qu'il occupe au barreau. Aucune preuve non plus quant à la part, s'il y en est, que la Couronne a reçue des $100,000 d'amendes. A prime abord, le dossier n'indique pas que des services légaux requérant plus d'habileté ou d'effort que d'ordinaire ont été rendus par le pétitionnaire.

Je considère que le pétitionnaire a, en toute connaissance et volontairement, consenti à un contrat par lequel le ministre ou sous-ministre de la Justice exerce de larges pouvoirs discrétionnaires lui permettant de fixer le montant de son compte. Donc, à moins de preuve suffisante pouvant justifier une conclusion que le préposé à la taxation avait agi de mauvaise foi ou que le montant tel que taxé n'était pas raisonnable, je ne crois pas devoir le modifier.

Pour les motifs susmentionnés, je ne puis que rejeter la pétition; cependant, vu le malentendu susmentionné entre les membres du Ministère de la Justice et le pétitionnaire, je suis d'avis que la pétition doit être rejetée sans frais.

Jugement en conséquence.

1960

Oct. 11, 12, 13

1961

Sept. 27

BETWEEN:

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

AND

HARRY EDGAR MORDEN ..... RESPONDENT.

Revenue—Income—Income tax—Betting—When winnings subject to income tax—The Income Tax Act, R.S.C. 1952, ss. 3, 4 and 127(1)(e).

The respondent, a hotel proprietor, in the years 1949 to 1953 inclusive, won substantial sums by betting on card games and sporting events. The Minister in reassessing the respondent added these sums to the taxpayer's declared income. The latter's appeal from the assessment was allowed by the Income Tax Appeal Board. On an appeal by the Minister to this Court

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Held: That to be taxable under the *Income Tax Act* a gambling gain must be derived from the carrying on of a "business" within the meaning of that term as defined by s. 127(1)(*e*) of that Act.

2. That as there was no evidence that the taxpayer, during the years in question in relation to his betting, had conducted an enterprise of a commercial character, or had organized these activities as to make them a business, calling or vocation, the appeal should be dismissed. *Down v. Compston* (1937) 21 T.C. 60, *Jones v. Federal Commissioner of Taxation* [1932] 2 A.T.D. 16 and *Lala Indra Sin, In re,* [1940] 8 I.T.R. 187 at 218, followed. *Partridge v. Mallandaine* (1886) 18 Q.B.D. 276, *Graham v. Green* (1925) 9 T.C. 309, referred to. *M.N.R. v. Walker,* [1952] Ex. C.R. 1, distinguished.

APPEAL under the *Income Tax Act.*

The appeal was heard before the Honourable Mr. Justice Cameron at Sarnia.

J. L. Lunney and *J. A. Gamble* for appellant.

W. A. Donohue, Q.C. for respondent.

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

CAMERON J. now (September 27, 1961) delivered the following judgment:

The Minister of National Revenue appeals from a decision of the Income Tax Appeal Board dated October 26, 1956[1] which allowed the respondent's appeals from re-assessments made upon him for the taxation years 1949, 1951, 1952 and 1953. In the re-assessments, all dated September 13, 1954, the Minister added to the declared income of the respondent the following amounts:

1949	$ 1,500.00
1951 (reduced by the Minister's Notification from $10,250.00)	10,000.00
1952	860.00
1953	1,500.00

The re-assessments indicated that the amounts so added were in relation to net gains from gambling activities. In Part B of the Minister's Notice of Appeal, it is alleged merely that these amounts were properly taken into account in computing the respondent's income for the years in question, that for the year 1953 being under the provisions of ss. 3 and 4 of *The Income Tax Act* and the

[1] 16 Tax A.B.C. 81; 56 D.T.C. 513.

others being under the provisions of the same sections of the 1948 *Income Tax Act*. The reply to the Notice of Appeal is merely a denial of these allegations.

The sections so referred to were 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.

* * *

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;

Although the Minister is the appellant, the onus of proving the assessments to be erroneous is on the taxpayer-respondent (*M.N.R. v. Simpson's Ltd.*[1]).

In 1935 the respondent acquired the Morden Hotel in Sarnia, Ontario, and operated it thereafter until 1957, when it was sold. He was assisted in the operation of that hotel, first by his son who died in 1952, and thereafter by a manager. His own evidence makes it abundantly clear that for a very considerable period of time the operation of the hotel was not his only, or possibly even his main, business interest. From about 1942 to 1948 he was the owner of a racing stable, having at times as many as twelve horses. A very substantial portion of his time was directed to training and racing these horses at many tracks in Canada and the United States and it is clear that throughout that period he was continuously placing bets on his own and other horses, paying a good deal of attention to racing information, attending the races, and gambling on horse races in a large way. For a long period of time he appears to have been an inveterate gambler, placing bets not only on horse races, but on a variety of card games and sporting events. He was a member of the Omega Club in Toronto where betting for heavy stakes was at least permitted and

[1] [1953] Ex. C.R. 93

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in which he participated. No records of his betting gains or losses was kept at any time. In 1948 he disposed of all his horses and, with the exception of one horse which he owned for a short time about 1952, has owned no race horses since that date.

His gambling activities up to the year 1948 were so extensively organized and occupied so much of his time and attention that, had they continued throughout the years in question, any net gain therefrom might possibly have been income from a business within the definition of "business" contained in s. 127(1)(*e*). It is submitted, however, that from 1949 to 1955, a period which includes all the taxation years in question, his gambling activities were only occasional and amounted to nothing more than indulging in a hobby or recreation, and that therefore his net income therefrom was not taxable.

The first question that arises is whether the respondent has established that the amounts added to his declared income were derived from gambling. As I have noted, the re-assessments all indicate that they were made on the basis that such was the case. There is no suggestion that he had any source of income other than from his hotel business and gambling or that his income from the operation of the hotel was incorrect. While the respondent and his witnesses in many cases were not clear as to dates and amounts of gambling gains and losses, I am satisfied (after taking into consideration the fact that the events occurred from seven to eleven years before the hearing of the appeal) that the evidence is sufficient to establish that the amounts so added represented, in fact, the net gain from gambling activities for the respective years in question. The respondent stated that to the best of his knowledge the amounts were correct and there is no evidence to deny it.

The remaining question is whether such gains are part of the respondent's taxable income.

Professional bookmakers accepting bets on race horses are taxable on the profits of what has been held to be their vocation (see *Partridge v. Mallandaine*[1].) I think it would follow, also, that persons who make gains by organizing their efforts in the way that a bookmaker does are deriving income which is taxable.

[1] (1886) 18 Q.B.D. 276.

In the well-known case of *Graham v. Green*[1], Rowlatt J. pointed out the distinction between the position of a bookmaker and the individual who bets with a bookmaker. In that case, the appellant for many years made substantial gains by betting on horses from his private residence with bookmakers at starting prices only. It was proven that that was his main, if not his sole, means of livelihood. Rowlatt J., in holding that his winnings were not profits or gains assessable to tax, said that a winning bet was substantially in the same position as a gift or finding. At p. 313 ff. he said:

> Now we come to betting, pure and simple. (I do not mean to say that mercantile bargains are tainted with the element of gambling.) It has been settled that a bookmaker carries on a taxable vocation. What is the bookmaker's system? He knows that there are a great many people who are willing to back horses and that they will back horses with anybody who holds himself out to give reasonable odds as a bookmaker. By calculating the odds in the case of various horses over a long period of time and quoting them so that on the whole the aggregate odds, if I may use the expression, are in his favour, he makes a profit. That seems to me to be organising an effort in the same way that a person organises an effort if he sets out to buy himself things with a view to securing a profit by the difference in what I may call their capital value in individual cases.
>
> Now we come to the other side, the man who bets with the bookmaker, and that is this case. These are mere bets. Each time he puts on his money, at whatever may be the starting price. I do not think he could be said to organise his effort in the same way as a bookmaker organises his. I do not think the subject matter from his point of view is susceptible of it. In effect all he is doing is just what a man does who is a skilful player at cards, who plays every day. He plays to-day and he plays to-morrow and he plays the next day and he is skilful on each of the three days, more skilful on the whole than the people with whom he plays, and he wins. But I do not think that you can find, in his case, any conception arising in which his individual operations can be said to be merged in the way that particular operations are merged in the conception of a trade. I think all you can say of that man, in the fair use of the English language, is that he is addicted to betting. It is extremely difficult to express, but it seems to me that people would say he is addicted to betting, and could not say that his vocation is betting. The subject is involved in great difficulty of language, which I think represents great difficulty of thought. There is no tax on a habit. I do not think "habitual" or even "systematic" fully describes what is essential in the phrase "trade, adventure, profession or vocation." All I can say is that in my judgment the income which this gentleman succeeded in making is not profits or gains, and that the appeal must be allowed, with costs.

In a later case, *Down v. Compston*[2], Lawrence J. decided that the respondent, a professional golfer who for a period of ten years habitually engaged in private game of golf for bets of varying amounts (and as often as three or four

[1] 9 T.C. 309.
[2] 21 T.C. 61.

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times a week) and made net profits from such bets up to £1,000 a year, was not assessable to tax in respect thereof. He held that the winnings did not arise from his employment or vocation and that he was not carrying on a business of betting. He found that there was no more organization in that case than there was in the case of *Graham v. Green* (*supra*).

In *M. N. R. v. Walker*[1], the taxpayer was a farmer actively engaged in farming. He also owned race horses and for a period of ten years regularly attended race horse meetings at a number of race tracks, spending about six weeks in each year at such meetings. He was assessed on a net worth basis, but claimed that in part his net worth had increased by reason of winnings from race horse betting. Hyndman, D. J. came to the conclusion that the taxpayer had not successfully established that he had won the amounts he claimed from horse race betting, but that even if he had, he had probably embarked on a business to make profits from betting on horse races.

In *Jones v. Federal Commissioner of Taxation*[2], where there appears to have been a conspicuous absence of system, and the element of sport, excitement and amusement were the main attractions, Evatt J. decided that Jones was not engaged in business, summing up his view as follows:

> All that I have said can best be summed up by saying that, during the relevant period, the appellant acquired and developed a bad habit which he was in the special position to gratify. I do not think that the gratification of this habit was a carrying on of any business on his part, despite his many bets and his heavy losses.

To be taxable, a gambling gain must be derived from carrying on a "business" as that term has been defined in s. 127(1)(*e*) (*supra*). Casual winnings from bets made in a friendly game of bridge or poker or from bets occasionally placed at the race track are, in my view, clearly not subject to tax. As stated by Hyndman, D.J. in the *Walker* case, each case must depend on its own particular facts. A reasonable test in such matters seems to be that stated in *Lala Indra Sen, In re*[3], where Braund, J. said at p. 218:

> If there is one test which is, as I think, more valuable than another, it is to try to see what is the man's own dominant object—whether it was to conduct an enterprise of a commercial character or whether it was primarily to entertain himself.

[1] [1952] Ex. C.R. 1. [2] [1932] 2 A.T.D. 16.
[3] [1940] 8 I.T.R. (Ind.) 187.

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In the present case, I find no evidence that the respondent during the years in question in relation to his betting activities conducted an enterprise of a commercial character or had so organized these activities as to make them a business calling or vocation. After he sold his horses in 1948, he lost practically all interest in horse racing and placed only an occasional bet on such races on the few occasions when he attended the tracks at Detroit. True, he was an inveterate gambler and was prepared to place a bet on the outcome of baseball, hockey and football matches, and on card games, whether he was a player or merely placed side bets. His main winnings were on the few occasions when he attended the Grey Cup football play-offs in Toronto, where he placed bets on the game and also played cards for substantial stakes with friends or acquaintances at the Omega Club, at the hotel, or at the homes of his friends, or placed side bets on other card players. In Sarnia he was accustomed to playing card games for small stakes on Wednesday afternoons with friends who gathered in the basement of a nearby store. While his bets were high at times and his gains substantial, I can find no evidence that his operations amounted to a calling or the carrying on of a business. Gambling was in his blood and it provided him with the excitement which he craved. It was his hobby. In the words of Rowlatt, J. in the *Graham* case (*supra*), "he was addicted to gambling" and it was his hobby, but for the years in question it was not his vocation, calling or business.

While there is evidence that in 1955 and thereafter he regained his interest in horse racing and indulged more frequently in placing bets thereon, I cannot see that that has any bearing on the facts as I have found them to be for the taxation years in question.

For these reasons, the appeal will be dismissed and the decision of the Income Tax Appeal Board affirmed. The respondent is entitled to his costs after taxation.

Judgment accordingly.

1960
June 20, 21, 22, 23
1961
July 5

BETWEEN:

CHARLES YEATES & COMPANY LIMITED ..... PLAINTIFF;

AND

INDEPENDENT GROCERS' ALLIANCE DISTRIBUTING COMPANY LIMITED ..... DEFENDANT.

Trade Marks—Infringement—Passing off—Whether trade marks "Royal Gold" and "Royal" confusing—Whether "Royal" a "common laudatory epithet" or "clearly descriptive or misdescriptive" word mark—"Similar"—"Distinctive"—Trade Marks Act, S. of C. 1952-53, c. 49, ss. 2(b), (f), 6(1)(2)(5), 7, 18(1)(a)(b), 18(2). 19, 20—The Unfair Competition Act, R.S.C. 1952, c. 274, s. 2(f)(k)(o).

In 1953 the plaintiff, who had been using the word "Royal" as a trade mark extensively and continuously in association with its products since 1922, obtained registration of the word as a trade mark for use in association with ice cream, ice cream sundries, milk, cream, buttermilk, cottage cheese, chocolate dairy milk, evaporated milk and condensed milk. The defendant in 1957 registered the trade mark "Royal Gold" for use in association with butter, ice cream, eggs and cheese slices. In an action for infringement and passing off the plaintiff sought an order to amend the defendant's registration by striking out therefrom the words "Royal" or "Royal Gold". The defendant counterclaimed for an order striking out the plaintiff's registration of the word "Royal" for use in association with ice cream.

Held: That having regard to the considerations mentioned in s. 6 of the *Trade Marks Act*, and the principles set out in *British Drug Houses Ltd. v. Battle Pharmaceuticals*, [1944] Ex. C.R. 239 (affirmed [1946] S.C.R. 50), the defendant's mark "Royal Gold" is not confusing with the plaintiff's mark "Royal" within the meaning of the *Trade Marks Act* and does not infringe any right flowing from its registration.

2. That since the evidence disclosed no act or conduct on the part of the defendant contrary to the prohibitions contained in s. 7 of the *Trade Marks Act*, the claim for passing off fails.

3. That as applied to goods the word "royal" is not a common laudatory epithet, nor is it "clearly descriptive or misdescriptive" of the quality of goods so as to fall within the prohibition of s. 26(1)(*f*) of the *Unfair Competition Act*.

4. That the mark "Royal" was not "similar" within the meaning of the *Unfair Competition Act* to "Royal Purple", "Royal Oxford", "Royal African", "Mount Royal", "Royal Canadian" or "Royal Scarlet", which were already on the register in respect of some of the same or similar wares at the time of the plaintiff's registration was not objectionable on that ground.

5. That, in seeking expungement of the plaintiff's registration under s. 18(1)(*b*) of the *Trade Marks Act*, the onus was on the defendant to show that at the time of the commencement of the proceedings the plaintiff's mark "Royal" was not distinctive and, as this onus has

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not been discharged, the defendant's claim failed. *Great Tower Street Tea Co. v. Smith*, 6 R.P.C. 165; *Coca-Cola Co. of Canada v. Pepsi-Cola Co. of Canada*, [1940] S.C.R. 17; *R. DeMuths Application*, 44 R.P.C. 27, distinguished.

ACTION for infringement and passing off. Counterclaim for an order striking out registration of plaintiff's trade mark.

The action was tried before the Honourable Mr. Justice Thurlow at Ottawa.

F. A. Brewin, Q.C. and *Ian Scott* for plaintiff.

Harold G. Fox, Q.C. and *D. F. Sim* for defendant.

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

THURLOW J. now (July 5, 1961) delivered the following judgment:

In this action the plaintiff claims an injunction and other relief for infringement of its registered trade mark "Royal" and for passing off by the use by the defendant of the trade mark "Royal Gold" and an order amending the defendant's registration of the latter mark by striking out therefrom the words "Royal" or "Royal Gold." The defendant counterclaims for an order striking out the plaintiff's registration of the trade mark "Royal" for use in association with ice cream.

The plaintiff is an Ontario corporation and since 1922 has carried on business in Guelph as a manufacturer of dairy products. In that year it began using the word "Royal" as a trade mark and has used it continuously ever since, chiefly in association with ice cream and ice cream products, which it has advertised extensively and sold in substantial volume in southern Ontario. The mark has been and is used in association with ice cream of superior quality, which commands a higher price on the market than inferior grades of ice cream. The plaintiff also manufactures a lower grade of ice cream, which it markets at a lower price, using in association therewith the word "Regal". In the area in which the plaintiff's products are marketed, it has been the practice of shopkeepers to handle only one manufacturer's ice cream, and the plaintiff, besides supplying material advertising its ice cream, has been accustomed to lend to the retailers by whom its products

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are sold refrigerators or cabinets in which to store its products, on the understanding that only products of its manufacture would be stored therein, the purpose apparently being to ensure that only the plaintiff's ice cream would be sold at these shops.

In 1947 the plaintiff applied for and ultimately in 1953 it obtained registration of the word mark "Royal" for use in association with ice cream and ice cream sundries, milk, cream, buttermilk, cottage cheese, chocolate dairy milk, evaporated milk, and condensed milk. At the time of the plaintiff's application, there were already on the register some 72 registrations of trade marks which either consisted of the word "Royal" alone or included that word in combination with another or others, all for use in association with food products of one kind or another or products in some way associated with food. Eight of these registrations consisted of the word "Royal" alone and were made between 1878 and 1932. By virtue of one registration of its own and assignments of six others, by 1946 seven of these eight registrations stood in the name of Standard Brands Ltd. and together were for use in association with baking powder, yeast powder, prepared mixes for cake, muffins and pie crust, yeast cakes, baking soda, flavouring extracts, cream of tartar, starch (not including laundry starch or rice starch), puddings, pie fillings, desserts, mayonnaise, 1000 island dressing, and other salad dressings, and sandwich spread. Between 1947 and the commencement of this action, these seven registrations or some of them had been amended to include, as well, corn and other cereal chips, margarine, tea, coffee, cocoa, mixes for preparing soft drinks, jelly mixes, mixed nuts, pecans, soup base for soups, and seasonings. The other registration of "Royal" prior to the plantiff's application was that of Worcester Salt Co., obtained in 1925, for use in association with salt and salt compounds. The rights under this registration were assigned to Morton Salt Co. of Illinois in 1948. Of the registrations of "Royal" in conjunction with some other word or words, only that of "Mount Royal" in 1933 specifically referred to ice cream, though "Royal Purple" purported to be in respect of "human foods other than tea" and "Royal Table" purported to include in its list "any other food and all alimentary products." Of the others, "Royal Oxford" included cheese,

"Royal African" included condensed milk, "Mount Royal" included milk, cream, buttermilk, and cheese, "Royal Canadian" included evaporated milk, condensed milk, and cream in tins, and "Royal Scarlet" included cheese.

The defendant is an organization which licenses wholesale grocery distributors to operate under its name, using methods and procedures which it has developed, including its merchandising and advertising programs. The distributors in turn license retail grocery stores in their areas to use the IGA name and promote their sales by the IGA methods. In 1954, through its licensed distributors the defendant began using the mark "Royal Gold" in association with eggs, ice cream and cheese slices, the products so marked being sold in substantial volumes in numerous outlets in Canada, including some 40 stores in the area in which the plaintiff's products are sold. In 1957 the defendant applied for and obtained registration of "Royal Gold" as a certification mark to be used in association with butter, ice cream, eggs and cheese slices. In 1959 the plaintiff discovered in three of the stores which were handling its products ice cream bearing the mark "Royal Gold", and in one of these stores the ice cream so marked, as well as ice cream bearing the plaintiff's mark, was in a refrigerator or cabinet which the plaintiff had provided. The plaintiff, through its solicitor, thereupon demanded that the defendant stop using its mark in association with products of the kind manufactured by the plaintiff and, upon the defendant's refusing or failing to comply, brought the present action.

At the trial, evidence was given by Mr. John A. Kitchen, a dealer in creamery and ice cream machinery and supplies carrying on business in Toronto, that to him the word "Royal", when used in association with ice cream, meant that the ice cream was of the plaintiff's manufacture. This witness had suggested the adoption of "Royal" by the plaintiff as its mark in 1922, and he had from time to time supplied refrigeration equipment to the plaintiff. Another witness, Mr. Alfred Hales of Guelph, stated that to him the word "Royal" in any context, when associated with ice cream, means the plaintiff's ice cream. He is a dealer in frozen foods, he handles the plaintiff's ice cream, and it does not appear that he buys or sells the ice cream of any

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other manufacturer. It is probable that to these witnesses the association of the word "Royal" with the plaintiff would be particularly strong. The only other witness called on behalf of the plaintiff was Charles Yeates, the president and principal shareholder of the plaintiff company, who gave evidence of the extent of the advertising and use of the mark by the plaintiff.

I turn first to the question whether the use by the defendant of the mark "Royal Gold" in association with ice cream infringes any right of the plaintiff which flows from its registration of the mark "Royal". By s. 19 of the *Trade Marks Act*, S. of C. 1952-53, c. 49, subject to certain exceptions to which it is unnecessary to refer, registration of a trade mark in respect of any wares gives to the owner the exclusive right to the use throughout Canada of such trade mark in respect of such wares, and by s. 20 the right of the owner of a registered trade mark to its exclusive use is deemed to be infringed by a person not entitled to its use under the Act who sells, distributes, or advertises wares or services in association with a confusing trade mark. "Confusing", when applied as an adjective to a trade mark, is defined by s. 2(b) as meaning a trade mark the use of which would cause confusion in the manner and circumstances described in s. 6. The relevant portions of s. 6 are as follows:

> 6. (1) For the purposes of this Act a trade mark . . . is confusing with another trade mark . . . if the use of such first mentioned trade mark . . . would cause confusion with such last mentioned trade mark . . . in the manner and circumstances described in this section.
>
> (2) The use of a trade mark causes confusion with another trade mark if the use of both trade marks in the same area would be likely to lead to the inference that the wares or services associated with such trade marks are manufactured, sold, leased, hired or performed by the same person, whether or not such wares or services are of the same general class.
>
> (5) In determining whether trade marks . . . are confusing, the court or the Registrar, as the case may be, shall have regard to all the surrounding circumstances including
>
> (*a*) the inherent distinctiveness of the trade marks . . . and the extent to which they have become known;
>
> (*b*) the length of time the trade marks . . . have been in use;
>
> (*c*) the nature of the wares, services or business;
>
> (*d*) the nature of the trade; and
>
> (*e*) the degree of resemblance between the trade marks . . . in appearance or sound or in the ideas suggested by them.

As a mark, "Royal" has, I think, some, but not much, inherent distinctiveness. The word is used both alone and in combinations with other words as the mark or part of the mark applied to a wide variety of goods by different traders to distinguish their goods from those of others. Because of this, "Royal" by itself, in my opinion, constitutes at best a weak mark, offering no wide range or field of distinctiveness for any particular trader. The mark "Royal Gold" has, to my mind, greater inherent distinctiveness, but I would class it, too, as a weak, rather than a strong mark. "Royal" has, however, been in use by the plaintiff in association with its products and, in particular, its ice cream for some 37 years preceding the commencement of this action, and I think it may be inferred that it has become well known to the public as the mark of the plaintiff's ice cream in the area in which the plaintiff's products are sold. "Royal Gold" has also been in extensive use for a period of time which, though much shorter, is also a substantial period, and I think it may safely be assumed that it, too, has become well known as a mark. The products in association with which both parties use these marks are items of food and are thus of a kind which are repeatedly purchased. The purchasers of such goods, in my opinion, generally know the trade marks on the goods they desire and are readily able to recognize differences in the marks. In this situation, it is a striking fact that, notwithstanding the use of both marks in the same area over a substantial period, the plaintiff could offer no evidence of any instance of actual confusion having occurred between its wares and those of the defendant or its licensees. Moreover, while there is some resemblance between these two marks in appearance and sound and there seems to be, as well, some resemblance in the ideas suggested by the two marks, I am of the opinion that anyone even vaguely aware of the plaintiff's mark would be struck more by the difference than by any resemblance between it and "Royal Gold" and would not be likely to regard "Royal Gold" as indicating the same source as "Royal", though it might cause some persons, and particularly those most familiar with the plaintiff's business and the nature of the defendant's operations, to wonder if the wares bearing the mark "Royal Gold" might not have been manufactured and packed by the plaintiff for the

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defendant. This, however, is far from producing a belief or an inference that the goods marked "Royal Gold" are those of the plaintiff. Having regard to the considerations mentioned in s. 6 of the *Trade Marks Act*, as well as to the principles set out in the judgment of the President of this Court in *British Drug Houses Ltd. v. Battle Pharmaceuticals*[1], which were recently referred to and applied by him in this Court in *Sealy Sleep Products v. Simpson Sears Ltd.*[2] and which I see no reason to repeat here, I have come to the conclusion that the use by the plaintiff of "Royal" and by the defendant of "Royal Gold" in the area in which the plaintiff's products are sold is not likely to lead to the inference that the wares associated with such trade marks are manufactured or sold by the same person. The defendant's mark "Royal Gold" is, accordingly, not confusing with the plaintiff's mark "Royal" within the meaning of that term in the *Trade Marks Act* and does not infringe any right flowing from its registration.

It follows that the plaintiff's claim, so far as it is based on infringement of its registered mark, must fail. And since the only ground advanced at the trial for striking out or amending the defendant's registration of "Royal Gold" was that "Royal Gold" is confusing with the plaintiff's registered mark, it follows that this claim fails, as well.

The plaintiff's claim for relief is also based on alleged passing off by the defendant through its licensees of their goods as goods of the plaintiff. As already mentioned, however, there is no evidence that anyone has ever purchased ice cream or any other product bearing the mark "Royal Gold" in the belief that it was manufactured by the plaintiff, and in the circumstances described there is, in my opinion, no practical likelihood of this occurring. As already indicated, the use of the mark "Royal Gold" is, in my view, not likely of itself to cause such an erroneous belief and, having regard to the fact that this mark appears on the defendant's packages preceded by the letters "IGA" in prominent type, whereas the plaintiff's packages state that the product is that of Charles Yeates and Co. Ltd., and to the many differences in the decoration of the pack-

[1] [1944] Ex. C.R. 239; [1946] S.C.R. 50.
[2] June 2, 1960. Unreported.

ages, as well as the difference in price, I do not think there is any likelihood of anyone mistaking the one product for the other or thinking, when he buys "Royal Gold" ice cream, that he is buying the product sold by the plaintiff as "Royal" ice cream. In fact, the only important feature the contending packages appear to have in common is the word "Royal", which, while it may tend to remind some people of the plaintiff, is in the whole of the circumstances, in my opinion, not calculated to lead to an inference or belief that the products marketed by the defendant or its licensees are products of the plaintiff. The plaintiff may well be troubled by the prospect that it may lose business through the abandonment by some shopkeepers of the practice of handling only one manufacturer's ice cream in their stores, but in my opinion the evidence discloses no act or conduct on the part of the defendant or its licensees contrary to the prohibitions against unfair competition contained in s. 7 of the *Trade Marks Act*. This ground, as well, accordingly fails as a basis for any of the relief claimed.

It remains to deal with the defendant's counter claim for expungement of the plaintiff's registration of "Royal" in respect to ice cream. At the trial, this registration was attacked on the ground that it was invalid both under clause (*a*) of s. 18(1) of the *Trade Marks Act* as having been not registrable at the date of its registration and under clause (*b*) of the same subsection as being not distinctive at the time of the commencement of these proceedings.

Section 18 of the *Trade Marks Act* provides:

18. (1) The registration of a trade mark is invalid if

(*a*) the trade mark was not registrable at the date of the registration;

(*b*) the trade mark is not distinctive at the time proceedings bringing the validity of the registration into question are commenced; or

(*c*) the trade mark has been abandoned; and subject to section 17, it is invalid if the applicant for registration was not the person entitled to secure the registration.

(2) No registration of a trade mark that had been so used in Canada by the registrant or his predecessor in title as to have become distinctive at the date of registration shall be held invalid merely on the ground that evidence of such distinctiveness was not submitted to the competent authority or tribunal before the grant of such registration.

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It follows from s. 18(1)(*a*) that a registration is invalid if the mark was not registrable at the time of its registration unless the registration can be saved under s. 18(2). It may be noted here that no attempt was made to support the registration under s-s. (2).

The law in force relating to registration of trade marks at the time of the plaintiff's registration of "Royal" was the *Unfair Competition Act*, by s. 26 of which it was provided that a word mark should, subject as otherwise provided in the Act, be registrable if it met certain conditions therein enumerated, one of which was that it should not be "to an English or French speaking person clearly descriptive or misdescriptive of the character or quality of the wares in connection with which it is proposed to be used, or of the conditions of, or the persons employed in, their production, or of their place of origin." By s. 2(*o*) a word mark was defined as meaning

> a trade mark consisting only of a series of letters and/or numerals and depending for its distinctiveness upon the idea or sound suggested by the sequence of the letters and/or numerals and their separation into groups, independently of the form of the letters or numerals severally or as a series.

Section 2(*m*) defined trade mark as follows:

> "Trade mark" means a symbol which has become adapted to distinguish particular wares falling within a general category from other wares falling within the same category and is used by any person in association with wares entering into trade or commerce for the purpose of indicating to dealers in, and/or users of such wares that they have been manufactured, sold, leased or hired by him, or that they are of a defined standard or have been produced under defined working conditions, by a defined class of persons, or in a defined territorial area, and includes any distinguishing guise capable of constituting a trade mark;

In *Registrar of Trade Marks v. G. A. Hardie & Co. Ltd.*,[1] on an appeal from a judgment of this Court allowing an application pursuant to s. 29 of the Act for registration of a mark, notwithstanding the fact that it was clearly descriptive and thus unregistrable as offending s. 26, the majority of the Supreme Court of Canada held that the principle of the *Perfection Case, Joseph Crosfield's & Sons Ltd. Application*[2] that no amount of use of an ordinary laudatory epithet would be sufficient to take it out of the common domain and enable the user to have it registered as his trade mark under the *Unfair Competition Act* was

[1] [1949] S.C.R. 483 [2] (1906) 26 R.P.C. 837

applicable in determining the capability of a word to become "adapted to distinguish" and thus registrable under the *Unfair Competition Act*.

Kerwin J. (as he then was) said at p. 489:

It was not contended that if the Court came to the conclusion that "SUPER-WEAVE" was an ordinary laudatory expression the application should succeed, but in view of the argument addressed to us, it is advisable to state what appears to be the proper construction of s. 29 of the Act. The opening words of subsection 1 "notwithstanding that a trade mark is not registrable under any other provision of this Act" require one to examine the definition of trade mark in section 2(*m*). That definition states that "trade mark" means a symbol "which has become adapted to distinguish". While this wording differs from section 9 of the English Act in question in the Perfection Case, since in s. 9 "distinctive" is stated to mean "adapted to distinguish", no distinction should be drawn between the uses of the different tenses. Turning again to s. 29, while the Court is empowered to grant the declaration mentioned, notwithstanding that a trade mark is not registrable under any other provision of the Act, the original idea underlying such legislation, as it has been developed in England, should be followed here, with the result that, if a word is held to be purely laudatory, no amount of use or recognition by dealers or users of words as indicating that a certain person assumes responsibility for the character or quality of the merchandise would be sufficient to take such an expression out of the common domain and enable the user thereof to become registered as the owner of a trade mark under *The Unfair Competition Act*.

Taschereau J. said at p. 490:

With due respect, I cannot agree, as I believe that the compound word "Super-Weave" is a laudatory epithet, and is capable of application to the goods of anyone else. Of its very nature it is common property and cannot be made the subject of monopoly. It is used for the purpose of advertising the superior quality of the weaving of a particular commodity.

Estey J. said at p. 508:

The language and plan of our statute is substantially different from the *Trade Marks Act* of 1905 in Great Britain but in principle its provisions for registration are similar and in effect much the same. It has always been recognized in both the common and statute law of both countries that with respect to trade marks there are words of such common and ordinary use that no person should be permitted to adopt them as trade marks and thereby acquire the exclusive right or monopoly to the use thereof. Even if in a particular instance in relation to specific wares evidence established "distinctiveness in fact" there remained that larger consideration of public interest which prevented their classification as words "adapted to distinguish." No amount of use by an individual could defeat the public interest and make possible their adoption as a trade mark. In the present enactment Parliament has not only not indicated a change but has adopted the phrase "adapted to distinguish" well known in the law of Great Britain under which this very principle is protected. Its meaning and position in Great Britain would be presented to Parliament in the adoption of this phrase, and, indeed, it might with

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propriety be suggested that the language was for that very reason adopted. In any event, a survey of the relevant sections and of the statute as a whole lead to the conclusion that the phrase "adapted to distinguish" has the same meaning in our statute as under the statute of Great Britain. It follows that words commonly used and appropriately described as laudatory epithets cannot become registrable as trade marks.

The same principle had previously been held applicable by this Court under the same Act in the *Hardie* case, as well as in *C. Fairall Fisher v. British Columbia Packers Ltd.*[1] and in *Standard Stoker Co. Inc. v. Registrar of Trade Marks.*[2]

The first objection to the plaintiff's registration advanced by counsel for the defendant was that "Royal" is a purely laudatory epithet registration of which was contrary to the principle applied in the *Hardie* case and that, in any event, "Royal" is a descriptive word, registration of which was contrary to s. 26(1)(*c*) except upon an application pursuant to s. 29, which was not made.

The word "Royal" has a variety of meanings and senses which depend on the context in which it is used. In some usages, it refers to some association or connection with the sovereign, in others to royal patronage, and in still others it appears to be simply a name, as when applied to a sail or a mortar or part of an antler. On the other hand, the *Shorter Oxford Dictionary* also gives among its meanings those of befitting, appropriate to, a sovereign, stately, magnificent, splendid; noble, first-rate. When used in this sense, "royal" is undoubtedly a laudatory adjective. To my mind, however, this is not a common but an infrequent usage of the word except in certain expressions such as "a royal welcome," and in this sense one rarely, if ever, finds this word chosen to praise or describe the quality of goods. Notwithstanding the statements by some of the witnesses that to them "Royal" on a product signified a good product, in my opinion, when the word "Royal" alone is used in this country in association with goods, and particularly goods such as ice cream and other dairy products, it is not used as an adjective and is not generally regarded as an adjective. It indicates neither connection with the sovereign nor royal patronage, nor does it impress me as referring to the quality of the goods. It is only when one's mind dwells at length on what it could mean that a possible

[1] [1945] Ex. C.R. 128 [2] [1947] Ex. C.R. 437

reference to quality suggests itself. As applied to goods, I would accordingly not regard "royal" as a common laudatory epithet which cannot on the principle applied in the *Hardie* case become registrable as a trade mark. Nor for the same reasons do I think "royal" is "clearly descriptive or misdescriptive" of the quality of the goods so as to fall within the prohibition of s. 26(1)(*f*) of the *Unfair Competition Act*.

The second objection upon which counsel for the defendant submitted that the plaintiff's mark was not registrable at the time of its registration was that it was similar to other word marks already registered for similar wares and its registration was, therefore, contrary to s. 26(1)(*f*) of the *Unfair Competition Act*. In support of this submission, counsel pointed to the registrations of "Royal Purple", "Royal Oxford", "Royal African", "Mount Royal", "Royal Canadian" and "Royal Scarlet" in respect to various foods, including in one or another ice cream and most of the other products named in the plaintiff's registration, and he took the position that in each case these were registrations in respect of wares in whole or in part similar to the wares referred to in the plaintiff's registration and that, if "Royal Gold" and "Royal" were confusing marks, "Royal" was similar to these other marks and should not have been registered.

In my opinion, the question whether "Royal" was registrable or not at the time of its registration is not to be resolved by reference to whether "Royal Gold", when registered, was "confusing" with "Royal" within the meaning of the *Trade Marks Act* but by the proper application of the statutory provisions in effect at the time of the plaintiff's registration of "Royal". Moreover, even if the statutory provisions then and now in effect were identical, it would not necessarily follow that the result of comparing "Royal" with other registered marks containing the word "Royal" would be the same as from comparing "Royal" with "Royal Gold" for each mark must be considered on its own. Section 26(1)(*f*) of the *Unfair Competition Act* was as follows:

> 26. (1) Subject as otherwise provided in this Act, a word mark shall be registrable if it
>
> (*f*) is not similar to, or to a possible translation into English or French of, some other word mark already registered for use in connection with similar wares . . .

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And by s. 2(*k*) it was enacted that:

2. In this Act, unless the context otherwise requires:—

* * *

(*k*) "Similar," in relation to trade marks, trade names or distinguishing guises, describes marks, names or guises so resembling each other or so clearly suggesting the idea conveyed by each other that the contemporaneous use of both in the same area in association with wares of the same kind would be likely to cause dealers in and/or users of such wares to infer that the same person assumed responsibility for their character or quality, for the conditions under which or the class of persons by whom they were produced, or for their place of origin;

In my opinion, while there may in some and perhaps all cases have been some similarity of wares within the meaning of s. 2(*l*) of the *Unfair Competition Act*, "Royal" was not similar, within the meaning of s. 2(*k*), to any of the marks "Royal Purple", "Royal Oxford", "Royal African", "Mount Royal", "Royal Canadian" and "Royal Scarlet", and its registration was not objectionable on that ground.

The other main ground of the defendant's attack on the plaintiff's registration was that the word "Royal" was not distinctive at the time of the commencement of these proceedings. In support of this ground, it was urged that the word "Royal" is common to the trade, and reference was made to the judgment of North J. in *Great Tower Street Tea Co. v. Smith*[1] and to the judgments of the Supreme Court of Canada and the Privy Council in *Coca-Cola Co. of Canada Ltd. v. Pepsi-Cola Co. of Canada Ltd.*[2] In my opinion, neither of these cases is of much help in considering the present problem. In the *Tower Tea* case, the court was considering the words "not in common use" which appeared in the applicable statute. In the *Coca-Cola* case, the word "Cola" was considered to be common to the trade, but the registration of "Coca-Cola" was not expunged. And in *R. Demuth's Application*[3], which was also cited, registration of "Seda Seltzer" was granted despite the opposition of the owner of "Alka-Seltzer", even though the word "Seltzer" was held to be common to the trade. The issue here, as I see it, is whether the mark "Royal" at the time of the commencement of these proceedings was distinctive, the onus of showing that it was not distinctive

[1] 6 R.P.C. 165 [2] [1940] S.C.R. 17; 59 R.P.C. 127

[3] (1948) 65 R.P.C. 342.

resting on the party attacking the registration. On this issue, evidence that the mark was common to the trade, either in the sense of being in common use in the trade or in the sense of being open to the trade to use by reason of its being a word commonly used to describe the goods, would in my opinion tend to show lack of distinctiveness, but descriptiveness is not necessarily incompatible with distinctiveness (*vide* Fletcher Moulton L.J. in the *Perfection* case[1]) and it must, I think, be kept in mind that the question to be answered is not whether the mark was common to the trade in either of these senses but whether, on the whole, the mark as registered was distinctive at the time of the commencement of the proceedings. By s. 2(*f*) of the *Trade Marks Act*, "distinctive" in relation to a trade mark is defined as meaning "a trade mark that actually distinguishes the wares or services in association with which it is used by its owner from the wares or services of others or is adapted so to distinguish them." Whether or not a trade mark actually distinguishes wares in association with which it is used by its owner from those of others is a question of fact depending on the circumstances disclosed in evidence. *Vide* Lord Dunedin in *Re the Application of F. Reddaway & Co. Ltd.*[2]

That the word "Royal" is employed widely as part of the names of many different businesses, both within and beyond those having to do with food, and that it forms part of many trade marks is abundantly clear. In some of these usages, particularly where it is used as an adjective qualifying another word or words with which it is used, it appears to have some meaning, but for the most part in these usages the word, in my opinion, is practically, if not entirely, meaningless and, while vaguely suggesting splendour, in fact suggests nothing descriptive of the business or firm or its wares or services. As used by the plaintiff in association with its wares, the word "Royal", in my opinion, is not descriptive of the quality of the goods, even though in the case of ice cream it is used by the plaintiff only in association with a product of superior grade and, as already

[1] (1909) 26 R.P.C. 837 at 857. [2] (1927) 44 R.P.C. 27.

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indicated, in my view it is not a word in common use in trade for the purpose of describing the quality of wares. The mark is accordingly not common to the trade in that sense.

Nor, in my opinion, is "Royal" in such common use in the trade as to be incapable on that account of being distinctive. As a mark, I regard the word "Royal" by itself as substantially different from the marks in evidence consisting of combinations of words which include it, and for this reason I think the use of the word in such combinations may be eliminated. The evidence shows that "Royal" is registered as the trade mark of Standard Brands Ltd. for a considerable number of staple grocery products and that it is in use as the trade mark of that company on at least one product, namely Royal Instant Pudding. It is also registered as the trade mark of Morton Salt Co. for salt and salt compounds, and there has been an application pending since June 6, 1952 for its registration as the mark of Gauthier & Tremblay Ltd. of Chicoutimi for use in association with meat, bacon, sausage, ham, etc. In addition, the evidence shows that there are or have been on the market biscuits, eggs, and furniture produced by different companies but all bearing the word "Royal" as a trade mark, and I see no reason to doubt that there may be others as well. On the other hand, the word has been in use as a trade mark by the plaintiff continuously since 1922 in the particular area of this country in which its products are marketed, and the extent of such use and the advertising which the plaintiff has done have, I think, been calculated to cause this mark to become well known in that particular area as the mark of the plaintiff and as indicating that these particular products, when so marked, are of the plaintiff's manufacture. The evidence of Mr. Hales, in my opinion, supports this inference. Nor is it shown, and this I think is of some importance, that any other producer uses this particular mark on the same products either in the area in which the plaintiff's goods are sold or elsewhere in Canada. On the whole, therefore, I am of the opinion that the word "Royal" has not been shown to be in common use in connection with products of the kind produced by the plaintiff or in the dairy trade, nor is it established that this mark, when used by the plaintiff in association with its ice cream and other products in the

area in which its products are sold does not actually distinguish such wares from those of others, within the meaning of the first part of the definition of "distinctive" in the statute. The defendant has, accordingly, failed to establish that the plaintiff's mark was not distinctive at the material time, and the objection to the plaintiff's registration on this ground, as well, therefore fails.

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The action and the counter claim will be dismissed, both with costs.

Judgment accordingly.

BETWEEN:

DONALD C. BROWN ..... APPELLANT;

AND

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

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Apr. 22, 23

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Aug. 15

Revenue—Income tax—Income Tax Act, S. of C. 1948, c. 42, s. 14(1) and the Income Tax Act, R.S.C. 1952, c. 148, s. 85B(1)(b)—Capital or income—Profit on real estate transaction—Assessment on a cash received basis.

Appellant with ample funds on hand in the form of negotiable securities, borrowed from his bank for the purpose of purchasing a lot in the City of Vancouver intending to build a small hotel on the land in order to set up his son in business. Shortly after the acquisition of the property he sold it at a profit.

Respondent assessed the appellant for income tax on the profit resulting from this transaction and from that assessment appellant appealed to this Court contending that such profit is capital gain.

Appellant also in partnership with another entered into an agreement with two wholesale grocers to erect a warehouse on property leased from the C.P.R. and rent to the wholesalers. This was done and the transaction provided a large profit to the appellant who appealed from an assessment for income tax on that profit and from the manner in which it was made.

Held: That the profits realized by appellant from both deals are income and assessable for income tax and such assessment to be in accordance with the provisions of the law regulating taxation of income returns accepted on a cash received basis as set forth in s. 14(1) of the *Income Tax Act*, S. of C. 1948, c. 42 and s-s. (1), Para. (*b*) of s. 85B of the *Income Tax Act*, R.S.C. 1952, c. 148.

APPEAL under the *Income Tax Act*.

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BROWN v. MINISTER OF NATIONAL REVENUE

Dumoulin J.

The appeal was heard before the Honourable Mr. Justice Dumoulin at Vancouver.

C. C. Locke, Q.C. and *W. M. Carlyle* for appellant.

G. S. Cumming and *T. E. Jackson* for respondent.

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

DUMOULIN J. now (August 15, 1961) delivered the following judgment.

This is an appeal from a decision of the Tax Appeal Board, dated the 27 day of May 1959, which affirmed two re-assessments made by the Minister of National Revenue, whereby the amount of appellant's net income for taxation year 1951 was increased by $5,000, and the net income for 1954 by the addition of a sum of $28,041.13.

Mr. Donald Cameron Brown, of Vancouver, B.C., has, for many years, been engaged, on an equal basis, with a partner, in the flour milling business under the name and style of Wild Rose Mills Ltd.

In 1951 and again in 1954, this appellant made two transactions which he looks upon as capital investments, whilst, on the other hand, the respondent would have them considered as dealings in real estate, constituting income from a business within the meaning attributed to that word in the *Income Tax Act*.

Two old houses, situate at the intersection Burrard and Smythe Streets, in Vancouver City, were purchased in late May or early June, by Donald C. Brown, as a promising opportunity for his son, a former airman, now engaged in the hotel and restaurant trades. The price paid was $40,000, borrowed at 4½ per cent interest from the Royal Bank of Canada; the purchaser electing not to disturb his holdings of $150,000, of which $130,000 consisted in government bonds.

Brown testified that he intended building a small 25-room hotel, with a possibility of enlarging it should conditions so require. This plan, however, was not disclosed to Brown, junior, before being carried out in May or June of 1951 as already noted.

A few days after he acquired this property, an agent of a car washing concern, Miss Mary Brooks, approached Brown, and asked if he would consider selling his very

recent purchase. Corroborating this statement, Miss Brooks (now Mrs. de Angelis) went on to say that: "We (her firm) earnestly considered going along with the project of building a small hotel with the financial assistance of Mr. Brown as we could not do so on our own".

An offer of $45,000 was finally accepted by D. C. Brown; the terms of payment being $10,000 in cash, and the $35,000 balance by monthly instalments of $100 from August 1, 1951, to September 1, 1955, the residue of $30,000 to be paid in a lump sum on August 1, 1961, with interest at 10 per cent a year in the meantime, payable each month.

Some adverse conditions, for instance the hum and vibration engendered by the car washing machinery, militated against the idea of erecting a hotel or rooming establishment over the cleaning garage.

Nevertheless, the deed of sale was duly completed and signed by all parties concerned on July 30, 1951, or two months after Brown had acquired the ownership (cf. exhibit 1).

Re-assessed as to his profit of $5,000, for taxation year 1951, the appellant objects that the originating transaction was not entered into . . ."pursuant or in relation to any class of profit-making operation . . . but (was) . . . acquired by the appellant to hold as investment" (cf. Statutory Provisions upon which the appellant relies, s. 1(*c*)).

It is a well known proposition, frequently re-asserted, that most cases under the Income Tax law are borderline ones, to be decided in the light of their own particular circumstances, the venerable fount of this practical wisdom being the Lord Justice Clerk's speech in the 1904 suit of *Californian Copper Syndicate v. Harris*[1].

Although not necessarily conclusive by themselves, the tests applied to a deal usually focus in the proper direction that ambiant light just mentioned.

If it is trite but true to say that an "investment" in contradistinction to "speculation", gives rise to a corollary notion of at least a relatively "long term" duration, then such an ear-mark does not apply to real estate bought in June 1951 and resold a few weeks later, July 30. Then again, there may be something in the fact that Brown chose to borrow $40,000 from the bank, when he could have

[1] (1904) 5 T.C. 159.

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acquitted the debt out of his own funds. I believe it would have seemed more consonant with the alleged intent of setting up his son in business had Brown engaged in this venture a requisite portion of his capital, rather than solicit a call loan from a bank.

The appellant also told the Court that the hotel or motel business was doomed to failure without a liquor permit and suggested three reasons why he could not hope to get one: firstly, on account of the impossibility of competing with the neighbouring hotels; secondly, because no licenses are granted in the vicinity of a school, and a large one was located nearby; thirdly because he, Brown, was not interested in this particular trade. Serious considerations no doubt, but as easily ascertainable before as after the transaction. Apparently, the weight of evidence fails to substantiate the appellant's contention and falls short of rebutting the statutory presumption which s. 42(6) of the *Income Tax Act* (11-12 Geo. VI, Ch. 52, 1948) decreed in favour of the respondent. I must then look upon this $5,000 gain as the yield of a profit-making scheme and consequently assessable for income tax purposes.

This point solved, another difficulty comes to the fore. Section 10 of the Notice of Appeal, applying to both the latter deal and the Taylor Street one, *infra,* raises the following objection:

> 10. At all times material to this appeal, the Appellant has reported his income on a cash received basis.

Section 9 of the "Reply to Notice of Appeal" does not admit this allegation, reaffirmed in the appellant's testimony and allowed to remain uncontradicted. Furthermore, in its Notice of Appeal, the appellant specifically relies, *inter alia,* upon s. 14(1) of the *Income Tax Act,* S.C. 1948, Ch. 42, hereunder cited:

> 14(1). When a taxpayer has adopted a method for computing income from a business or property for a taxation year and that method has been accepted for the purposes of this Part, income for the business or property for a subsequent year, shall, subject to the other provisions of this Part, be computed according to that method unless the taxpayer has, with the concurrence of the Minister, adopted a different method.

The Court, satisfied that appellant's plea on this matter was fully vindicated by the evidence, must then proceed to apportion the income tax due for 1951 on the basis of cash receipts.

At the hearing, in the assumption that such a finding might ensue, the respondent agreed "on principle" that:

1. The proportion of the $5,000 profit received in 1951 is the amount that the cash proceeds paid in 1951 bear to the total sale price, eg.
   The total sale price was $45,000.
   The portion thereof received in 1951 was $10,500.
   The calculation is:

$$\frac{\$10,500 \times 5,000}{\$45,000} = \$1,166.66$$

2. The same principle would be applied in subsequent years and the profit would be allocated on the same basis.

Accordingly, Donald C. Brown's net income for taxation year 1951 should be raised by adding to it a sum of $1,166.66 only, instead of $5,000.

The Taylor Street Lease.

We now reach the second ground on which the instant appeal rests.

It will be remembered, as said at the start of these notes, that Brown exploited a flour milling enterprise, jointly with a partner. In 1948, their company, "Wild Rose Mills Ltd.", leased from the Canadian Pacific Railway, for a ten years' duration, renewable for a similar period, some vacant land along Taylor Street, Vancouver City, on which Brown and his associate Weaver erected a warehouse they subquently rented to Wild Rose Mills Ltd.

Some years later, two wholesale grocers, Messrs. Fong and Tim Louie, inquired of Brown whether he and a now different partner for that particular enterprise, one Helge Pearson, would build for them a 40,000 square feet storage shed on an adjacent lot, belonging to the CPR, but under a rental option to Brown.

This offer was accepted and by November of 1953, the warehouse completed and delivered to the Louie Brothers, the land lease, however, persisting in the name of the joint builders, of whom, one, Helge Pearson, was a contractor by trade. Exhibit "5", dated August 1, 1954, a statement of adjustment, has, for its first entry the following: "To purchase price: $170,000", that, to all intents, may be taken to be the total cost of the 40,000' warehouse, with, probably though unrevealed at trial, an additional consideration for the assignment, July 31, 1954, of the ground lease by Brown and Pearson to the Louies, for the balance of a term of 10

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years from the first day of July, 1953 (cf. ex. 6). On July 31, 1954, the residuary sum still owing by Fong and Tim Louie amounted to $86,397.74, secured by a corresponding mortgage, executed also on July 31, 1954 (cf. ex. 7).

Under oath, Donald C. Brown testified that this deal brought in an over-all profit of $56,000, his one half share being $28,000, which, we know, was added to his net income for 1954.

Appellant's interest in the transaction, namely $85,000, or one half of $170,000, was payable to him . . . "as to the sum of $41,801.13 by cash or by way of adjustments, and as to the balance of $43,198.87 by 119 consecutive monthly instalments of $359.99, commencing on the 1st day of August, 1954, and ending on the 1st day of June, 1964, plus one final instalment of $360.06 on the 1st day of July, 1964, together with interest . . ." (cf. para. 8 of the Notice of Appeal).

The transaction at issue comprises two elements: 1. the erection of a storage shed, 2. the assignment of a nine-year lease, both, of course, for a profit.

Of these, the construction of a building in partnership with a professional contractor, working in the regular line of his calling, the ownership reverting to a third party, the Louie Brothers, is hardly reconcilable with a long term investment, if one does not confuse the venture itself with its terms of payments. If I may use such an expression, all the traditional lineaments of a speculation are vividly outlined in this commercial operation. Its second element, assignment of the lease, a mere right of temporary possession, a *jus ad rem* instead of a *jus in re*, hardly falls in the investment class. Here again, as in the Burrard Street case, we are confronted with a venture in the nature of trade, conformably to the definition that s. 139(1)(*e*) of the *Income Tax Act* (R.S.C. 1952, ch. 148) gives of the expression "business". Consequently any profit accruing therefrom to the taxpayer is liable to income taxation in keeping with ss. 3 and 4 of our Act.

A knottier difficulty in this instance is whether or not the entire gain of $28,041.13 was properly added by respondent to the taxpayer's net income for the one year, 1954? It is of record that Brown's annual income returns were made

and accepted on a cash received basis: Exhibit 7 stipulates 120 monthly instalments for payment of the balance owing to wit: $43,198.87. For 1954, the cash receipts and adjustments were $41,801.13 out of a total owing to Brown of $85,000 (*vide* Notice of Appeal, para. 8). Surely the appellant cannot be denied the elementary right of recouping his costs, or $56,958.87, before figuring on any profit, and the acknowledged returns, by cash and adjustments, for the material year left a gap of $15,157.74 between costs and profits (i.e. $56,958.87—$41,801.13=$15,157.74).

The respondent, virtually conceding the incongruity of its initial taxation, now says in para. 14 of its Reply to Notice of Appeal, that . . . "he is prepared to re-assess the Appellant for his 1954 taxation year so as to allow him as a deduction the sum of $13,657.32 pursuant to paragraph (*d*) of subsection (1) of section 85B".

This statutory enactment relates to . . . "property sold in the course of the business" of a taxpayer, in relation to which the amount included "in computing the income from the business for the year or a previous year . . . is not receivable until a day

(i) more than two years after the day on which the property was sold, and

(ii) after the end of the taxation year."

In the instance foreseen by s. 85B(1)(*d*) "there may be deducted a reasonable amount as a reserve . . . for the unpaid balance of the profit". However close to a solution this may appear, I am inclined to think that para. (*b*) of s-s. (1) of 85B is closer still, and I quote its text:

> 85B (1) In computing the income of a taxpayer for a taxation year,
>
> (*b*) every amount receivable in respect of property sold or services rendered in the course of the business in the year shall be included notwithstanding that the amount is not receivable until a subsequent year unless the method adopted by the taxpayer for computing income from the business and accepted for the purpose of this Part does not require him to include any amount receivable in computing his income for a taxation year unless it has been received in the year. (underlinings are mine.)

Section 85B, s-s. (1)(*d*), it would seem, is applicable when the method of accounting provided by 85B(1)(*b*), may not be properly resorted to. On this score, my opinion is strengthened by the schedule suggested in connection with the Burrard Street sale and accepted by both parties.

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In the latter instance, then, as in the former, the proportion of the $28,000 profit, received in 1954, should be the amount that the cash proceeds paid in 1954 bear to appellant's share ($85,000) of the total sale price. The record being referred back to the respondent for rectification, it is unnecessary that I should affix the figures consequential to the above equation.

In brief, the appellant fails in his contention that the Burrard and Taylor Streets transactions were meant as investments; they were on the contrary ventures in the nature of trade, pursuits of so many profit-making schemes, legitimately liable to income tax.

On the other hand, appellant's claim that for the material years, 1951 and 1954, he should be assessed on a cash received basis, appears justified and admissible. Therefore s. 14(1) of the *Income Tax Act,* 1948, and s. 85B, s-s. (1)(*b*) of the 1952 Act, should govern the annual ratio of taxation. The circumstances of the suit do not warrant the allocation of costs to either party.

For the reason given this Court doth order and adjudge that the sum of profits realized by appellant in the Burrard and Taylor Streets deals are assessable to income tax, but in accordance only with the provisions of the law regulating taxation of income returns accepted on a cash received basis, being ss. 14(1) of both the 1948 and 1952 Acts, and s-s. (1) para. (*b*) of s. 85B, 1952. Appeal allowed in part.

The record will be returned to the Minister for the corollary rectification and apportionments of tax relative to taxation years 1951 and 1954. No costs.

Judgment accordingly.

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Feb. 23, 24

Oct. 3

BETWEEN:

ADOLFO LENDOIRO .....SUPPLIANT;

AND

HER MAJESTY THE QUEEN .....RESPONDENT.

Crown—Petition of Right—Crown Liability Act, S. of C. 1952-53, c. 30, s. 3(1)(a)—Post Office Act, R.S.C. 1952, c. 212, s. 40 and regulations—Damages claimed for loss of letter due to failure of clerk to place in

suppliant's post office box—"Mishandling of anything deposited in a post office"—Issue determined by provisions of Post Office Act and not by those of Crown Liability Act—Crown not liable.

Suppliant brings his petition of right to recover from the Crown damages allegedly suffered by him due to the failure of a postal clerk in a post office known as Station H in Montreal, Quebec, to place in a box in that post office rented by suppliant a letter containing a cheque for $12,000 which had been mailed to him at that address from Caracas, Venezuela, as a result of which he was unable to complete arrangements for shipping a large number of prize cattle to Venezuela.

Suppliant relies on s. (3), s.-s. (1), para. (*a*) of the *Crown Liability Act*, S. of C. 1952-53, c. 30.

Respondent denies that suppliant suffered damages due to negligence of an employee and pleads s. 40 of the *Post Office Act*, R.S.C. 1952, c. 212 and the regulations made thereunder.

Held: That the suppliant is not entitled to any of the relief claimed in the petition of right.

2. That s. 40 of the *Post Office Act* vests in the Crown the power or authority to determine by regulation to what extent, if any, it will be liable for claims arising from the loss, delay or mishandling of anything deposited in a post office, and that in the absence of anything to the contrary contained in the Act itself or its regulations no liability exists.

3. That the word "mishandling" in s. 40 of the *Post Office Act* means *inter alia* to handle badly, improperly or wrongly and accurately describes the error which was made in not placing the letter addressed to suppliant in the proper box in the post office. *Lever Brothers Co. Ltd. et al. v. The Queen*, [1960] Ex. C.R. 61; [1961] S.C.R. 189, distinguished.

4. That the issue raised in the case is to be determined by s. 40 of the *Post Office Act* and not s. 3(1)(*a*) of the *Crown Liability Act*.

PETITION OF RIGHT seeking to recover damages from the Crown allegedly suffered through the tortious act of a servant of the Crown.

The action was tried before the Honourable Mr. Justice Kearney at Montreal.

Kalman S. Samuels and *Mrs. Stella Samuels* for suppliant.

Roger Tassé for respondent.

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

KEARNEY J. now (October 3, 1961) delivered the following judgment:

This is an action in tort by way of petition of right wherein it is claimed that, due to the fault, negligence, imprudence and lack of care or skill of employees and officials of the Post Office Department while in the performance of the work for which they were employed, the

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suppliant has suffered damages to the extent of $24,299.50. The said damages allegedly arose out of the failure of those engaged at the post office known as Station H, Montreal, P.Q., whereat the suppliant had leased Post Office Box 335, to locate and deliver to him an important letter containing a cheque for $12,000 and which had been mailed to him at his above-mentioned address from Caracas, Venezuela, and as a result he was unable to complete arrangements for shipping a large number of prize cattle and suffered damages to the extent claimed.

The suppliant relies on section 3, subsection (1), paragraph (*a*), of the *Crown Liability Act* (1-2 Elizabeth II), 1952-53, c. 30, which states:

> The Crown is liable in tort for the damages for which, if it were a private person of full age and capacity, it would be liable in respect of a tort committed by a servant of the Crown.

The respondent denies that the suppliant suffered the damages claimed and alleges that such damages, if any, were not directly attributable to the fault of the respondent's servants; that, in any event, the relief sought by the petition of right is in respect of a claim arising from allegations of loss, delay or mishandling of something deposited in a post office; that neither the *Post Office Act,* R.S.C. 1952, c. 212, nor the regulations made thereunder contain any provision making Her Majesty liable for claims arising as aforesaid; that in consequence the suppliant's claim is barred by reason of section 40 of the said Act which reads as follows:

> Neither Her Majesty nor the Postmaster General is liable to any person for any claim arising from the loss, delay or mishandling of anything deposited in a post office, except as provided in this Act or the regulations.

The main facts of the case are as follows.

The suppliant is in the business of buying and selling cattle and previous to September 1958 had made shipments of Canadian cattle to purchasers in Caracas, Venezuela, including one J. M. Garcia, from whom the suppliant had a pending order for about 40 head of cattle which he was about to ship via the *S/S Romney,* due to leave Montreal on September 18. During the month of August the suppliant was in Europe and during his absence Alejandro Mujica, on the recommendation of Mr. Garcia, wrote to the

suppliant at Burnside Farms, Howick, Quebec, under date of August 14 (Ex. 6), informing him that his firm wished to import from Canada 100 Holstein cows of first class quality, to arrive in Venezuela from October 15 onwards, and asking for price quotations thereon. The above-mentioned letter remained unanswered until the suppliant's return, at the end of August, and on September 4 the suppliant immediately contacted Mr. Mujica by long distance telephone. During the telephone conversation Mr. Mujica agreed to purchase from the suppliant, on behalf of himself and his partner, one G. Hernandez, thirty Holstein cows at a price of $600 each. The suppliant requested Mr. Mujica to make a part-payment of $12,000 and to deposit it to the suppliant's order at the Royal Bank of Canada, which Mr. Mujica agreed to do.

As appears by Exhibit 4, which forms the basis of the present claim, on September 10 Mr. Mujica wrote the suppliant from Caracas, stating that, instead of placing $12,000 to the order of the suppliant in the Royal Bank of Canada, his associate, Mr. Hernandez, preferred to make a cheque drawn against The Chemical Corn Exchange Bank of New York to the suppliant's order for $12,000 (U.S. funds). Mr. Mujica posted the letter and cheque by ordinary mail addressed to Adolfo Lendoiro Seaone, Box 335 Station H, Montreal, Canada, as indicated on the envelope (Ex. 3). There appears on its face a line striking out the address and the word "Removed" written in black ink was added alongside it. Written in red ink by the sender is the word "Urgente", the Spanish equivalent of "Urgent", and stamped on the reverse side of the envelope are the words "Recherche—Directory 1212". There is no postmark on the envelope to indicate the date on which it was received at Station H, but it bears postmarks indicating that it was sent from Station H on September 17, 1958 to the Toronto Undeliverable Mail Office or Dead Letter Office, as it is more commonly called, where it was received on September 18. Exhibit 3 does not bear any return address, but the Dead Letter Office in Toronto returned it to the original sender, Mr. Hernandez, in Caracas, about two months later.

As later appears, the suppliant had occasion to go to Caracas in October and December 1958. At the time of his first visit, Exhibit 3 containing the original of Exhibit 4

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had not yet been returned to Mr. Hernandez; but, on that occasion, he gave the suppliant a copy of Exhibit 4, and on his second visit in December he obtained Exhibit 3 from Mr. Hernandez.

The suppliant's evidence shows that in August 1958 he expected to complete a sale with prospective buyers other than Messrs. Mujica and Hernandez for about 80 head of cattle for shipment to Caracas and had reserved a like number of stalls for the September 18 sailing of the *S/S Romney*. He procured a firm order from Mr. Garcia for 40 head of cattle, which he shipped by the *S/S Romney,* but the balance of the expected order did not materialize, and according to the suppliant, he would have been able to include the shipment of 40 head of cattle purchased by Mr. Mujica, but not having received the $12,000 cheque, he cancelled his reservations on the remaining available stalls and lost a profit of $12,000 on the Mujica sale, which he otherwise would have made.

In his original petition the appellant limited his claim to the sum of $12,000 above-mentioned. But due to the occurrences hereunder described, by amendment the amount was increased by an additional $12,299.50.

It was usual for the *S/S Romney* to take 12 to 15 days to reach Venezuela. During the last week of September, the suppliant flew to Caracas because he "had to go to Venezuela to receive this cattle", which he had shipped to M. Garcia. Before leaving Montreal for Caracas, the suppliant, if I correctly understand his evidence on the point—which is not clear—, had taken a verbal option through M. Tough of the March Shipping Company on shipping space for cattle on the next sailing on the *S/S Romney*; but, due to the loss of the $12,000 cheque and the uncertainty of being able to effect a sale to M. Mujica of 100 head of cattle, the suppliant gave up the above-mentioned option before leaving for Caracas. During his stay in Caracas, the suppliant completed a sale of 107 head of cattle to Messrs. Mujica and Hernandez at a price of $600 each. On his return to Montreal, on October 10, he endeavoured to procure shipping accommodation on the next sailing of the *S/S Romney* only to find that she was fully booked throughout the balance of the year. Other companies shipping from Montreal were likewise booked up. The best

he could arrange was to procure accommodation on a ship leaving from New York in November. The cost of doing so was considerably in excess of what he would have had to pay if he had shipped from Montreal. The 107 head of cattle arrived in poor condition and the purchasers, consequently, refused to pay the full sale price thereon; and, in addition, the suppliant allegedly suffered additional damage through loss of goodwill, the whole totalling $24,299.50—as appears by a statement of damages filed as Exhibit 14 and which he attributes to his failure to receive in proper time the $12,000 cheque contained in Exhibit 3.

The evidence shows that as soon as the suppliant became aware that the letter containing the cheque had left Caracas on September 10 he made unavailing inquiries at Station H, and he was advised by the Director of Postal Service for the district of Montreal that no trace of it could be found.

Mr. Elzéar Therrien, who was in charge of Postal Station H in Montreal in 1958, testified that it was difficult for him to understand why the letter in question was not deposited in Box 335 as it should have been. On being questioned about the markings on the envelope he said he could not be sure when the letter arrived at Station H. But he explained why it was sent to the Toronto Undeliverable or Dead Letter Office on the 17th of September. There are three undeliverable mail offices in Canada: one located in Vancouver, and its function is to trace undeliverable mail originating in the East or Far East; the Montreal office deals with undeliverable letters originating from Europe; and the Toronto office deals with those sent from South America, whence Ex. 3 (and its contents) was returned to the sender in Caracas. No attempt was made to explain the reason which likely motivated the clerk, whoever he was, to strike off the address and inscribe the word "Removed" on the envelope. I might here state, as I observed during the hearing, that Box 335 was rented in the name of Adolfo Lendoiro and the letter in question was addressed to Adolfo Lendoiro Seaone; hence, it is possible that the clerk focused his attention on the last name, and finding on inquiry that nobody named Seaone was, at that time, the lessee of a post office box, had presumed that he

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had changed his address. As those familiar with the customs and practices of Spanish-speaking countries are aware, a man is described not only by his Christian name or names followed by his surname, but after the surname the maiden name of his mother is added. When he was sworn as a witness, the suppliant gave "Seaone" as his last name, while in his action he describes himself in the Canadian fashion as Adolfo Lendoiro. He is also thus described in letters in the record sent to his addresses in Howick (Ex. 6) and in Montreal (Exs. 9 and 17), and I do not think it is unreasonable to infer that the Latin American fashion in which he was described on Exhibit 3 served to confuse the clerk who first dealt with the letter.

It is true that two letters (Exs. 1 and 2) which were addressed: Adolfo Lendoiro Seaone, Station H, Box 335, Montreal, were there delivered to him, but they are postmarked "October 13" and "December 13, 1958" respectively, which is subsequent to the frequent occasions on which the suppliant alerted those in charge of Postal Station H by complaining that an important letter was missing.

Even supposing it could be said that the suppliant, in some measure, contributed to its own misfortune, would it follow that the servant of the Crown, and particularly the clerk in question, was blameless? As counsel for the suppliant observed, regardless of what prompted the clerk to deal with Exhibit 3 in the manner in which he did, it was a mistake for him not to place it in Box 335; and with this statement I am in full accord, more particularly as this error is admitted by Mr. Therrien, who, at the time, was in charge of Station H.

This leads to the important issue of whether by reason of s. 40 of the *Post Office Act* s. 3(1)(*c*) of the *Crown Liability Act* has any applicability in the present case.

It is submitted on behalf of the appellant that s. 3(1)(*c*) of the *Crown Liability Act* which came into force on November 15, 1953, if it did not completely supersede the exculpatory provisions of the *Post Office Act* which have been on the statute books for many years, at least placed decided limitations on the effect to be given to such provisions. It need hardly be said that the two Acts must be read together.

In this connection, counsel for the suppliant submitted that s. 3(1)(*a*) of the *Crown Liability Act* lays down the general rule that liability attaches to the Crown in the same manner as it does to ordinary citizens in respect of a tort committed by one of its servants, except in certain instances specifically mentioned in Act. Thus, for example, s. 3(4) states that notwithstanding s. 3(1) the liability of the Crown is limited by reason of certain provisions of the *Shipping Act*; similarly, s. 4(1) provides that no proceedings lie against the Crown if the claimant is entitled to a pension or compensation payable out of the Consolidated Revenue Fund; section 4(3) exempts the Crown from liability for damages sustained by any person, caused by a tort committed by a servant of the Crown while driving a motor vehicle on a highway, unless the driver of the motor vehicle or his personal representative is liable for the damages so sustained.

Counsel for the suppliant concluded from the foregoing that the *Post Office Act* was inapplicable because no mention is made of it among the foregoing exceptions. Assuming for a moment such to be the case, the following quotation from *Barker v. Edgar*[1] is found in Craies on *Statute Law*, 4th ed., p. 321:

> When the Legislature has given its attention to a separate subject and made provision for it, the presumption is that a subsequent general enactment is not intended to interfere with the special provision unless it manifests that intention very clearly. Each enactment must be construed in that respect according to its own subject-matter and its own terms.

Although it is true that the *Post Office Act* is not mentioned by name in the *Crown Liability Act*, I think it is referred to by implication in the provisions of subsection (6) of section 3, which reads, in part, as follows:

> Nothing in this section makes the Crown liable in respect of anything done or omitted in the exercise of any power or authority that, if this section had not been passed, would have been exercisable by virtue of the prerogative of the Crown, *or any power or authority conferred on the Crown by any statute*, ... (emphasis supplied)

I think the statutory provisions of section 40 of the *Post Office Act*, which was enacted in its present form by S. of C. 1940, c. 57, clearly vest in the Crown the power or authority to determine by regulation to what extent, if any, it will be liable for claims arising from the loss, delay or mishandling of anything deposited in a post office—and

[1] [1898] A.C. 748 at 754.

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that in the absence of anything to the contrary contained either in the Act itself or its regulations, no liability exists. The official guide of the Canadian Postal Service, 1961 (Ex. B) and the testimony of Elzéar Therrien indicate that no indemnity is made payable in connection with post office handling of ordinary mail; that the maximum indemnity to be paid on even a registered letter is $100 within Canada; that the amount payable in respect of claims relating to foreign mail, which is determined by treaty, varies; and, in the case of Canadian-Venezuelan treaty, it is limited to $3.75 per letter.

It was stated on behalf of the suppliant that his was not a claim arising from loss, delay or mishandling of the letter in question by servants of the Crown, as contemplated in the *Post Office Act,* but arose because they were guilty of tort of a much more serious character and which amounted to gross negligence on their part and with respect to which s. 3(1)(*a*) of the *Crown Liability Act* was intended to apply to the exclusion of s. 40 of the *Post Office Act.*

In this connection, counsel for the suppliant cited *Lever Brothers Company Limited et al.* and *Her Majesty the Queen*[1] confirming the judgment of Thurlow J.[2] which, in my opinion, is readily distinguishable from the present case because it was one in which the facts clearly indicated that the *Post Office Act* was inapplicable and because the facts in this case show the reverse to be true. In the *Lever* case a package of jewellery which was subject to duty had been transferred by the Canada Post Office into the custody and control of the Customs Postal Branch and while there was stolen by some employee or employees of such Branch during working hours and in the course of his or their employment. Thurlow J., who rendered the judgment in this Court, found that, under the circumstances, the Crown was liable for the loss; that neither s. 23(1) of the *Customs Act,* R.S.C. 1952, c. 58, nor s. 40 of the *Post Office Act,* R.S.C., 1952, c. 212 are applicable. As there is no suggestion that the *Customs Act* has any bearing on the present case, it can be disregarded. Speaking of the non-applicability of

[1] [1961] S.C.R. 189. [2] [1960] Ex. C.R. 61.

s. 40 of the *Post Office Act,* Ritchie J. delivering the judgment of the Supreme Court of Canada at page 193 observed:

> It was pointed out by counsel for the appellant that by s. 2(1)(*c*) of the same Act the words "deposit at a post office" are defined as meaning "to leave in a post office or with a person authorized by the Postmaster General to receive mailable matter" and that s. 2(2) provides that "an article shall be deemed to be in the course of post from the time it is deposited at a post office until it is delivered". . . . .
>
> In my view, at the time of the loss the diamonds in question were neither "deposited in a post office" nor "in the course of mail" and, accordingly, I agree with the learned trial judge that the provisions of s. 40 of the Post Office Act have no application to the present case.

In the present case there is incontrovertible proof that Exhibit 3 was left in Station H, a post office within the meaning of s. 2(1)(*i*), which states:

> 2. (1) In this Act,
>
> (i) "post office" includes any building, room, vehicle, letter box or other receptacle or place authorized by the Postmaster General for the deposit, receipt, sortation, handling or despatch of mail;

In the *Lever Brothers* case, it was unnecessary to determine, and the Court did not determine, what the outcome would have been had the package of jewellery been in the custody and under the control of the Post Office Department; and I do not think it is necessary for me to consider what the consequences might have been in the present case had Exhibit 3 and its contents been stolen by one of the postal clerks while it was lodged at Station H.

In my opinion, there is no comparison between the innocent mistake made by a postal clerk and the deliberate conversion to his own use by a customs employee of a package containing diamonds. In the *Lever* case the Court was concerned with a criminal act, while I consider that in the instant case the damages arose from duties attaching to the sorting of mail wherein clerical mistakes are almost bound to occur, much as occupational ailments are apt to afflict those engaged in certain exposed types of work.

Emilien Corbeil, district director of postal service for the Montreal postal district, who was called on behalf of the suppliant, stated that claims for loss of undelivered mail are made through his office and that the missing items consist of anything from a letter lost in the ordinary post to insured parcels. He testified that in his own district alone

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he receives an average of 50,000 to 60,000 complaints a year (Corbeil, p. 134). Elzéar Therrien (*supra*) stated that at Station H there are 14 clerks and two officers and that the average number of letters handled by the clerks per day are seventy-five to one hundred bags, of which three to four thousand letters are destined for the post office boxes in Station H, of which Box 335 is the last one. Mr. Corbeil (p. 35) stated that, although the Canadian Post Office system, in comparison with other countries, rates high, it is usual for two mistakes such as happened in the present case to arise in respect of each one thousand letters sorted.

It was submitted that, apart from the mistake which the sorting clerk made in respect of Exhibit 3 (on which, it should be recalled, the sender had omitted to place a return address), the fact that the postmaster was unable to trace it to the Dead Letter Office in Toronto, whence it was only returned to Caracas some time in November, constituted further acts of gross negligence on the part of servants of the Crown. In my opinion, in addition to the reasons above-mentioned these acts which followed the sorting clerk's original error may be disregarded, as they bear no direct relation to the damages claimed.

The suppliant raised the point that the word "mishandling" does not aptly describe the sorting clerk's error. Although it may mean maltreating or handling roughly, it also means to handle badly, improperly or wrongly (see *Shorter Oxford Dictionary,* 3rd ed., p. 1260; Webster's *New International Dictionary,* 2nd ed., p. 1569). And in my opinion it would be difficult to find any word which would more aptly and accurately describe the error which the sorting clerk made in failing to lodge Exhibit 3 in P.O. Box 335. For the above reasons, I consider that the provisions of s. 40 of the *Post Office Act,* and not s. 3(1)(*a*) of the *Crown Liability Act,* should be made to govern in the present case.

Because of the conclusion I have reached, I find it unnecessary to deal with any of the subsidiary issues raised in the case.

The petition of right will be, consequently, dismissed with costs.

Judgment accordingly.

1960
Sept. 27
1961
Aug. 4

BETWEEN:

ROSEMARY GERTRUDE HUSTON .....APPELLANT;

AND

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

AND BETWEEN:

FREDERICK B. WHITEHEAD .....APPELLANT;

AND

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

AND BETWEEN:

ELSE B. WHITEHEAD .....APPELLANT;

AND

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

Revenue—Income—Income Tax Act—Compensation award by War Claims Commission for World War II loss—Direction award bears simple interest—Whether sum referred to as "interest", capital or income—The Appropriation Act, No. 4, 1952, S. of C. 1952, c. 55—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 6(b) and 139(1)(ag).

The appellants in 1953 made application to the War Claims Commission for compensation for property owned by them in Czechoslovakia which was partially destroyed by the German Army in World War II. The Commission recommended payment out of the War Claims Fund to each of the appellants and that such amounts should bear simple interest from January 1, 1946 at the rate of 3% per annum. On October 10, 1958 this recommendation was approved by the Treasury Board and on October 17, 1958 cheques were forwarded the appellants' counsel by the Department of Finance together with a letter stating that the cheques enclosed represented the payments recommended by the War Claims Commission together with interest to October 10, 1958.

In assessing each of the appellants for the year 1958 the Minister added to the income reported by them the amount referred to as "interest" in the Commission's award. In an appeal from the assessments

Held: That the payments take their nature not from the motives for making them, or from what they are called, but from what in substance they are.

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2. That in the case of each appellant the amounts paid was a capital grant no part of which was "interest" or "received as interest" within the meaning of s. 6(*b*) of the *Income Tax Act*.

Glenboig Union Fireclay Co. Ltd. v. Commissioners of Inland Revenue, [1921] S.C. 400; [1922] S.C. (H.L.) 112; (1922) 12 T.C. 427; *Commissioners of Inland Revenue v. Ballantine*, (1924) 8 T.C. 595; *Simpson v. Executors of Bonner Maurice*, (1929) 14 T.C. 580; 45 T.L.R. 581, referred to. *Riches v. Westminster Bank*, (1947) 28 T.C. 159 distinguished.

APPEALS under the *Income Tax Act*.

The appeals were heard before the Honourable Mr. Justice Thurlow at Toronto.

C. H. Morawetz for appellants.

G. W. Ainslie and *F. J. Cross* for respondent.

THURLOW J. now (August 4, 1961) delivered the following judgment:

These are appeals from assessments of income tax for the year 1958. In that year, each of the appellants received a payment out of the War Claims Fund established pursuant to S. of C. 1952, c. 55, s. 3, vote 696, a portion of which payment has in each case been treated as income by the Minister in making the assessment under appeal, and the issue in all three appeals is whether the portion in question was income for the purpose of the *Income Tax Act*, R.S.C. 1952, c. 148.

The appellant Else B. Whitehead is the mother of the other two appellants, and all three have at all material times been Canadian citizens. Prior to World War II, each of them had owned an interest in a factory in Czechoslovakia which had been confiscated by the German authorities following the German occupation of Czechoslovakia in 1939. At the conclusion of the war in Europe, the confiscation and subsequent transfers of the property were treated as void, and the interests of the appellants in the factory were restored. The factory had, however, been partially destroyed by the German army a few days before the war ended.

In July, 1951, an Advisory Commission on War Claims, consisting of the Right Honourable J. L. Ilsley as sole commissioner, was appointed by the Government of Canada to inquire into and make recommendations respecting a number of subjects pertaining to claims arising out of

World War II in respect of death, personal injury, maltreatment, and loss or damage to property, including in particular among other matters that of whether interest should in any cases be allowed. By his report dated February 25, 1952, the commissioner recommended that a war claims fund be established and that there be transferred into it certain funds consisting of reparations available to Canada pursuant to agreement between certain of the governments of the countries which had participated in the war against Germany and certain funds and property held by the Custodian of Enemy Property, and he made many recommendations as to the categories of claims to be paid from the fund or to be denied payment therefrom and the principles and priorities to be applied in assessing the claims and ultimately paying them. Included in his recommendations was one that interest at 3% per annum from January 1, 1946 until the date of payment be included as an element of the amount to be paid in respect of property losses other than losses at sea.

Following this report, Parliament by the *Appropriation Act, No. 4, 1952,* S. of C. 1952, c. 55, s. 3, vote 696, granted a nominal sum

> To authorize
>
> (*a*) the Custodian of Enemy Property to transfer to the Minister of Finance such property, including the proceeds and earnings of property, that is vested in the Custodian in respect of World War II as the Governor in Council prescribes,
>
> (*b*) the Minister of Finance to hold, sell or otherwise administer property received by him from the Custodian under paragraph (*a*) or from other sources by way of reparations by former enemies (except Italy) in respect of World War II, and
>
> (*c*) the Minister of Finance to establish a special account in the Consolidated Revenue Fund to be known as the War Claims Fund, to which shall be credited all money received by him from the Custodian under paragraph (*a*) or from other sources by way of reparations by former enemies (except Italy) in respect of World War II, the proceeds of sale of property under paragraph (*b*), the earnings of property specified in paragraph (*b*) and amounts recovered from persons who have received overpayments in respect of claims arising out of World War II;
>
> and, notwithstanding section 35 of the *Financial Administration Act,* to provide for payments out of the War Claims Fund in the current and subsequent fiscal years, in accordance with regulations of the Governor in Council, to persons who claim compensation in respect of World War II for the payment out of the War Claims Fund in the current and subsequent fiscal years of expenses incurred in investigating and reporting on claims of those persons and for the repayment out of the War Claims Fund to Vote 128 (miscellaneous minor and unforeseen expenses) of all amounts

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that have been paid out of that Vote pursuant to The War Claims Interim Compensation Rules established by Order in Council, P.C. 667 of February 4, 1952.

Pursuant to this authority, the Governor in Council by Order in Council P. C. 4267 of October 9, 1952 established War Claims Regulations providing that the recommendations contained in the report of the Advisory Commission on War Claims, modified to the extent specified in the Schedule to the regulations, should constitute the rules governing payment out of the War Claims Fund of compensation in respect of war claims and that payment might be made out of the Fund with the approval of the Treasury Board to a person in respect of a war claim of an amount that, in the opinion of the War Claims Commissioner to be appointed pursuant to the Regulations, that person was eligible to receive under the war claims rules. By regulation 5, it was provided that "No right to payment is conferred by these regulations." In the schedule to the regulations, paragraph 5, entitled "Interest", provided:

Simple interest at three per centum per annum may be paid on the following classes of awards:

(*a*) For property losses on the high seas from the date of the loss;

(*b*) For personal injury or death on the high seas from the date of the loss;

(*c*) For disbursements for medical and similar expenses from the date of the disbursement; and

(*d*) For all other claims, excluding awards for maltreatment, from January 1, 1946.

These regulations were revoked and replaced by new regulations by Order in Council P. C. 1954-1809, but the provisions above mentioned remained unchanged in the new regulations.

Claims put forward by the appellants in respect of the damage to their interests in the Czechoslovakian factory were heard by the Deputy War Claims Commissioner, who on May 30, 1957 made a recommendation which was later reviewed and on August 23, 1958 approved by the Chief War Claims Commissioner. The latter recommended that there be paid to the claimants the following amounts as compensation for damage to properties in Czechoslovakia:

(*a*) To Mrs. Elsie B. Whitehead, $27,824.00, such payment to be in Orders of Priority Nos. 3(a) to 5 inclusive;

(*b*) To Mrs. Rosemary Huston, $37,098.00;

(*c*) To Frederick Whitehead, $37,098.00;

each of the two last payments to be in Orders of Priority Nos. 3(a) to 6(a) inclusive.

Each of the foregoing payments should bear simple interest from 1st January 1946 at 3% per annum.

On October 27, 1958, cheques were forwarded by the Department of Finance to the counsel who had appeared for the claimants in favour of Mrs. Else B. Whitehead in the sum of $38,487.83, in favour of Frederick Whitehead in the sum of $51,316.18, and in favour of Mrs. Rosemary Huston in the sum of $51,316.18, together with a letter stating that the cheques represented payment of the amounts recommended by the War Claims Commission, together with interest to October 10, 1958, the date on which payment was approved by the Treasury Board.

In making the assessments under appeal, the Minister added to the income reported by the appellants the amounts referred to as "interest", and he assessed tax accordingly.

The question to be determined is whether these amounts were income for the purposes of the *Income Tax Act*. Section 3 of that Act declares that the income of a taxpayer for the purposes of Part I is his income for the year from all sources and, without restricting the generality of the foregoing, includes income for the year from all (*a*) businesses, (*b*) property, and (*c*) offices and employments. Section 4 provides that, subject to the other provisions of Part I, income for a taxation year from a business or property is the profit therefrom for the year. And s. 6 provides that "without restricting the generality of s. 3 there shall be included in computing the income of a taxpayer for a taxation year . . . (*b*) amounts received in the year or receivable in the year (depending upon the method regularly followed by the taxpayer in computing his profit) as interest or on account or in lieu of payment of, or in satisfaction of interest."

The position taken by the Minister in support of the assessments was that the sums in question were interest and were income within the meaning of these provisions and the reasoning of the English courts in *Riches v. Westminster Bank*[1] was relied on as showing the income

[1] (1947) 28 T.C. 159.

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character of the payments in question. The appellants' position was that to call a sum interest does not make it interest or income within the meaning of the *Income Tax Act*, that what is to be determined in each case is the true character of the receipt and that the payments here in question, though called interest and calculated or measured as interest, were not interest in fact but were simply grants.

That the payments in question were not income from a business or from an office or employment within the meaning of the statutory provision above referred to is, I think, perfectly clear. And though it is perhaps not quite so clear, I am also of the opinion that the sums in question cannot properly be classed as income from property within the meaning of the same provision. "Property" is defined in s. 139(1)(*ag*) as meaning "property of any kind whatsoever whether real or personal or corporeal or incorporeal and without restricting the generality of the foregoing, includes a right of any kind whatsoever, a share or a chose in action." As I see it, the sums in question are not income from property because, notwithstanding the exceedingly broad scope of the statutory definition, the appellants during the period from January 1, 1946 to October 10, 1958 in respect of which the alleged "interest" was computed, in my opinion, had no property or legal or equitable right of any kind in the amount on which the alleged "interest" was computed. Nor, unless the payments were in fact "interest", do I see any other basis on which the sums in question could be regarded as income within the meaning of s. 3. The question to be determined is thus reduced to that of whether the "interest" payments in question are amounts required by s. 6(*b*) to be brought into the computation of the income of the appellants.

In approaching this question, it may be observed that, if amounts can be or become interest within the meaning of s. 6(*b*) merely by reason of what they are called, how they are computed and what they are intended to represent, there is no difficulty here, for the amounts were called interest, they were calculated at a yearly rate on a "principal" sum for a particular period of time, and they were obviously intended by Chief Justice Ilsley, and I think by every subsequent authority who dealt with the matter, to compensate the appellants in respect of their

not having had the "principal" amount from January 1, 1946 until October 10, 1958. Moreover, if the intention of the payer or even that of the payer and receiver were conclusive, I would have little difficulty in reaching the conclusion that the sums in question were paid and received as interest.

These features, however, to my mind are not only not conclusive but are liable to confuse and obscure the real issue. That issue is whether these amounts from the point of view of the appellants were "received as interest" within the meaning of s. 6(*b*). The name attached by the parties to payments, the way the amounts are calculated, and what they represent may often be of great importance in resolving such an issue, but the issue is one of substance and depends not on these features alone but on the other features of the case, as well. For just as a sum which is in truth interest, though called by some other name, will fall within the meaning of the section, so a sum which in truth is not interest, in my opinion, will not be "received as interest" within the meaning of the section, even though it may have the name and some of the other attributes of interest. To take the example suggested by counsel, it is, I think, plain that a legacy would not be "received as interest" within the meaning of s. 6(*b*) merely because the testator in his will had chosen to call it interest and had directed that its amount be computed by reference to a rate on a particular amount for the period between the making of the will and the testator's death.

Another example is *Glenboig Union Fireclay Co. Ltd. v. Commissioners of Inland Revenue*.[1] In that case, a sum to which the taxpayer was entitled in respect of the loss of one of its assets was computed by reference to the profit which might have been realized by the taxpayer in using the asset. The asset had, however, been one of a capital nature, and the taxpayer's entitlement being to compensation in respect of its loss, the amount awarded was held also to be capital, rather than profit or income. The fact that the amount was calculated by reference to the profits that might have been made and in a sense represented profits which the taxpayer had lost the opportunity to earn did not turn the receipt into one of an income nature.

[1] (1922) 12 T.C. 427.

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Similarly, in *Commissioners of Inland Revenue v. Ballantine*[1] a sum described as interest which was included in an award of "additional costs, loss and damages" was held to be simply part of the damages and not chargeable to tax.

In *Simpson v. Executors of Bonner Maurice*[2], an amount described and calculated as interest was awarded by a tribunal which was authorized under the Treaty of Versailles to award "compensation in respect of damage or injury inflicted upon" the property of the deceased. It was held that the amount was not interest or income. Rowlatt J., whose judgment was affirmed by the Court of Appeal, said at p. 593:

> The Treaty gave compensation, and the tribunal which assessed the principal sum has assessed it as interest. I think this sum first came into existence by the award, and no previous history or anterior character can be attributed to it. It is exactly like damages for detention of a chattel, and unless it can be said that damages for detention of a chattel can be called rent or hire for the chattel during the period of detention, I do not think this compensation can be called interest.

The situation in *Riches v. Westminster Bank* (*supra*) was quite different from that in the example, as well as from those in the cases cited and that in the present case. In the *Riches* case, what was held taxable was an amount awarded by a court pursuant to a statute authorizing the award of *interest*. It was awarded in respect of a sum which the plaintiff had had a legal right to receive many years earlier, and it was awarded as interest in respect of the intervening period. That the amount so awarded was of an income nature was on the whole reasonably clear, and the main question decided was not whether it had such a character but whether the fact that an award of interest in such circumstances was an award in the nature of damages for the detention of the principal sum was not compatible with it being regarded as income exigible to tax. The House of Lords held that there was not necessarily any incompatibility between the two conceptions. Viscount Simon put the matter thus at p. 187:

> The Appellant contends that the additional sum of £10,028, though awarded under a power to add interest to the amount of the debt, and though called interest in the judgment, is not really interest such as attracts Income Tax, but is damages. The short answer to this is that there is no essential incompatibility between the two conceptions. The real

[1] (1924) 8 T.C. 595.

[2] (1929) 14 T.C. 580.

question, for the purpose of deciding whether the Income Tax Acts apply, is whether the added sum is capital or income, not whether the sum is damages or interest.

Lord Simonds also said at p. 194:

> Here the argument is that, call it interest or what you will, it is damages and, if it is damages, then it is not "interest in the proper sense" or "interest proper", expressions heard many times by your Lordships.
>
> This argument appears to me fallacious. It assumes an incompatibility between the ideas of interest and damages for which I see no justification. It confuses the character of the sum paid with the authority under which it is paid. Its essential character may be the same, whether it is paid under the compulsion of a contract, a statute or a judgment of the Court. In the first case it may be called "interest" and in the second and third cases "damages in the nature of interest", or even "damages". But the real question is still what is its intrinsic character, and in the consideration of this question a description due to the authority under which it is paid may well mislead.

At the foot of p. 195, Lord Simonds also said:

> My Lords, having discussed in a general way the nature of a sum of money awarded as interest under section 28 of the Civil Procedure Act, I turn to the cases decided under the Income Tax Act to see whether they assist the appellant. I find in them just what I expected to find. The question in each case is whether the receipt is of an income or a capital nature; that is the test for Income Tax purposes, not whether it is called "interest" or "damages."

In the result, the House of Lords held, as had the High Court and the Court of Appeal, that the amount there in question was "interest of money" within the meaning of para. 1(*b*) of Schedule D of the *Income Tax Act, 1918*.

In the present case, as I see it, no question arises as to whether the amounts in question were damages or compensation, for they may be neither and yet not be taxable. The sole issue is whether the amounts were interest, but in resolving this issue the test to be applied is the same as that stated by Lord Simonds, namely, whether the amounts in question are of an income or a capital nature. The facts are that the appellant's property had been partially destroyed in 1945, a misfortune for which, so far as has been made to appear, they had no right to legal redress against anyone, and, in any event, none against the Government of Canada. *Vide Civilian War Claimants Association Ltd. v. The King.*[1] Despite what was going on in the meantime, that continued to be the legal position until October 10, 1958, when the Treasury Board approved

[1] [1932] A.C. 14.

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the payments, which were made to them shortly afterwards. No principal sum was payable in the meantime, nor was interest accruing on any principal sum, nor were the appellants being kept out of any sum to which they were entitled. In truth, during the whole of the intervening period they had no right to compensation for their loss, and there was neither interest accruing to them nor loss of revenue being sustained in respect to which they would be entitled to interest by way of damages or compensation.

In this connection, it may be noted that, while the House of Lords in *Riches v. Westminster Bank* overruled *Re National Bank of Wales*[1], it did not overrule *Commissioner of Inland Revenue v. Ballantine* or *Simpson v. Executors of Bonner Maurice, (supra)* both of which appear to me to be stronger cases in this respect than the present for attributing an income nature to the sums in question, since in these cases the taxpayer's right to the sum to which "interest" was added arose prior to or at the commencement of the period in respect to which the "interest" was computed. No case of which I am aware goes so far as to hold such an amount, call it interest or damages or compensation or any other name, to be interest or income when there was neither interest accruing in fact on the "principal" amount during the material period nor any right to the "principal" amount vested in the taxpayer during that period.

Moreover, notwithstanding the history of partial destruction of the appellant's property and the reasons which moved Parliament to set up the War Claims Fund and to "authorize" payments from it "in accordance with regulations" "to persons who claim compensation in respect of World War II" the payments so made appear to me to have been simply grants to individuals. They may be described as compensation for losses, they may be referred to in part as interest, they were undoubtedly made to these individuals because they suffered loss from the war and did not have their property intact at the end of the war, but to my mind the payments, like the legacy in the example and like the compensation awarded in *Glenboig Union*

[1] [1899] 2 Ch. 629.

Fireclay Ltd. v. Commissioner of Inland Revenue, take their nature not from the motives for making them or from what they are called, but from what in substance they are, in the example a legacy, in the *Glenboig* case statutory compensation for loss of a capital asset, in the present case grants. No doubt, under the War Claims Regulations, the amount of the grant in each case was to be in part measured or determined by reference to an interest calculation, and it may also be accepted that the reason for so measuring and granting such part was to offset an income loss, but the amount so arrived at was non-existent, it was nothing but a calculation and had no character at all until approved by the Treasury Board and, when so approved, it came into being "without previous history or anterior character" and was, in my opinion, simply the amount of a capital sum granted to the claimant. In my view, no part of the sum granted was of an income nature, and the amounts in question were, therefore, not "interest" or "received as interest" within the meaning of s. 6(*b*) of the *Income Tax Act.*

It was submitted in the course of argument that the fact that the payments were gratuitous payments by the Government of Canada would not render them inexigible to tax if they were in their nature income payments, and *Goldman v. Minister of National Revenue*[1] and *Severne v. Dadswell*[2] were cited as examples, the *Goldman* case as an example of a gratuitous payment being held to be income from an office and *Severne v. Dadswell* as an example of a gratuitous payment being held assessable as profit arising from a trade. In view of the conclusion which I have reached on the main question, it is unnecessary to consider this submission in detail, but it appears to me that the cases cited were simply applications of particular taxing enactments to particular facts and that no principle affecting the present situation is to be derived from them.

Finally, it was argued that, when a statute provides for the payment of interest, the word "interest" should be interpreted as having its natural meaning. The word

[1] [1953] 1 S.C.R. 211. [2] [1954] 3 All E.R. 243.

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"interest" does not, however, appear in *The Appropriation Act*, pursuant to which the payments were made. That Act simply authorized "payments" to particular persons in accordance with regulations to be made. The regulations made pursuant to this authority do refer to "interest", but that, to my mind, falls far short of a statutory enactment that the sums to be paid are interest.

The appeals will be allowed and the assessments varied accordingly in the case of Else B. Whitehead and Frederick Whitehead and vacated in the case of Rosemary Huston. The appellants are entitled to the costs of the appeals, the costs of the trial to be apportioned one third to each appellant.

Judgment accordingly.

BETWEEN:

JOHN ARCHIBALD McLEAN .....APPELLANT;

1959
Apr. 20, 21, 22

AND

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

1962
Jan. 16

Revenue—Income Tax Act 1948, S. of C. 1948, c. 52, s. 125(a)—Income Tax Act, R.S.C. 1952, c. 148, s. 137(2)—Income or capital gain—Failure to discharge onus of establishing Minister's assessment is wrong—Appeal dismissed.

In 1924, Prescription Optical Co. Ltd. (a British Columbia company) was incorporated by a number of ophthalmologists in Vancouver, its business being that of filling prescriptions for eye glasses. In 1931, all its tangible assets and the right to use its name were transferred to Imperial Optical Co. Ltd. which thereafter carried out all the operational functions of Prescription Optical Co. Ltd. The latter company, on certain conditions, had the right to re-purchase the tangible assets and, if it did so, Imperial Optical Co. Ltd. could no longer use the name of Prescription Optical Co. Ltd. Pursuant to an agreement then entered into with the individual doctor-shareholders, Imperial Optical Co. Ltd. thereafter paid the said shareholders a commission on all prescriptions referred to Prescription Optical Co. Ltd. by the shareholders. In 1936, the appellant was registered as the owner of one share in Prescription Optical Co. Ltd. and thereafter until March, 1946 received commissions on all prescriptions so referred by him and paid income tax thereon. In 1946, the *Medical Act* of British Columbia was amended and after April 11, 1946, it was illegal for any doctor in British Columbia to take or receive any such commissions.

In 1947, it was arranged that all the outstanding shares of Prescription Optical Co. Ltd. (24 in all) should be transferred to Standard Optical Co. Ltd.—a subsidiary of Imperial Optical Co. Ltd. Subject to certain conditions and adjustments it was agreed that Standard Optical Co. Ltd. should pay $320,000, that amount to be apportioned between the twenty then practicing shareholders of Prescription Optical Co. Ltd. in proportion to their referral of prescriptions to Prescription Optical Co. Ltd. during the three previous years, and that the payments so allotted should be made in ten equal annual instalments. The sum of $29,172.52 was allotted to appellant and it is admitted that in each of the years 1949 to 1953 he received $2,917.25, which amounts were added to his declared income for each of those years. An appeal to the Tax Appeal Board was dismissed and appellant now appeals to this Court. On behalf of the appellant it is submitted that the said sums were not income, but rather instalments of the purchase price of a capital asset, namely, the one share in Prescription Optical Co. Ltd.; and that all the shares were worth at least $320,000. For the Minister, it is submitted that the annual payments were taxable income on the alleged ground (*inter alia*) that part of the consideration for the price of the shares was the appellant's agreement to encourage his patients thereafter to have their prescriptions filled by Prescription Optical Co. Ltd.

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The Court was not satisfied that all relevant, available facts and documents relating to the transfers of the shares were put in evidence, particularly an agreement and letter signed by the appellant which formed "part of the consideration for the purchase and sale" of the shares. Other matters were not satisfactorily explained, such as (a) the agreement that if the appellant should die or retire from practice before the ten annual payments had been completed, Standard Optical Co. Ltd. would "pay one year's instalment plus *pro rata* for the number of months practiced since our previous payment", all the remaining instalments being cancelled; (b) the fact that the estates of three deceased shareholders, and one doctor who was about to retire, received no part of the purchase price.

Held: That the appellant had not discharged the onus which lies upon the taxpayer to establish that there is error in fact or in law in the assessments under appeal.

2. That the appeal must be dismissed.

APPEAL from the Income Tax Appeal Board.

The appeal was heard before the Honourable Mr. Justice Cameron at Vancouver.

The Honourable J. W. deB. Farris, Q.C. and *J. L. Lawrence* for appellant.

C. W. Tysoe, Q.C. and *T. E. Jackson* for respondent.

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

CAMERON J. now (January 16, 1962) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board dated September 25, 1957[1] dismissing the appellant's appeals from re-assessments dated May 13, 1955, for the taxation years 1949 to 1953, both inclusive. In reassessing the appellant, the respondent for each of those years added to his declared income $2,917.25, stated to be "payment by Standard Optical Co. Ltd. re transfer of shares of Prescription Optical Co. Ltd." The appellant admits the receipt of that amount in each year and the sole question for determination is whether such receipts were taxable income in his hands, or, as he submits, they were merely instalments of the sale price of a capital asset, namely, one share in Prescription Optical Co. Ltd.

In the course of this judgment, it will be necessary frequently to refer to three optical companies. For the sake of brevity, I shall refer to Prescription Optical Co. Ltd. as

[1] 18 Tax A.B.C. 43.

"Prescription"; to Imperial Optical Co. as "Imperial"; and to Standard Optical Co. Ltd. as "Standard". Imperial is a large optical company with headquarters at Toronto; its western manager at all relevant times at Vancouver was H. L. Boyaner. Standard is a wholly owned subsidiary of Imperial, its head office being at Toronto.

Prescription was incorporated as a private company under the *Companies Act* of the province of British Columbia in 1924 with a share capital of $10,000 divided into 10,000 shares of a par value of one dollar each. Its business at all times was mainly that of filling prescriptions for eye glasses; it did not, however, make or grind glasses, that being done by an optical company, presumably by Imperial. From the date of its incorporation until all the shares were sold in 1947 to Standard, the only shareholders were a number of eye specialists, or ophthalmologists in Vancouver. From 1924 to 1931 it would appear that such profits as were made were divided among the doctor-shareholders according to the number of shares each held and that the number of shares so held varied according to the number of prescriptions each had sent to Prescription.

In 1931, substantial changes took place. As shown by Exhibit D, the share capital was reduced to $3,565 divided into 3,565 shares of one dollar each and with "power to increase and divide into several classes, and to attach thereto respectively any preferential, deferred, qualified or special rights, privileges or conditions as to payment of dividends, distribution of assets, voting or otherwise". There is no evidence that the powers so conferred were ever exercised. Thereafter, all the issued shares were of the same class, namely, common shares of a par value of one dollar each. As of that date, there were fifteen doctor-shareholders, each holding one share, the remaining 3,550 shares being unissued.

On June 1, 1931, Prescription transferred all its tangible assets to Imperial (Exhibit 1) for the expressed consideration of $15,000. On June 3, 1931, an agreement was entered into between Prescription and Imperial (Exhibit 2). It contained certain provisions conferring on Imperial the right to use the corporate name of Prescription, but reserved to Prescription the right, by giving one week's notice, to repurchase the tangible assets of Prescription at any time and on certain terms, and that "in the event of such re-purchase

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the leave and right to use the name Prescription Optical Co. Ltd. . . . shall immediately cease and determine". From that date until the sale of the shares to Standard in 1947, all the business operations of Prescription were carried on by Imperial.

On June 3, 1931, Imperial sent the letter, Exhibit 3, to each of the doctor-shareholders of Prescription. Thereby, Imperial covenanted in consideration of the agreement (Exhibit 2) to supply monthly to each shareholder a complete statement of all prescriptions such shareholders had "directed to us through the Prescription Optical Co. Ltd., disclosing the invoice price of Prescription Optical Co. Ltd. and the retail sale price, all repairs to be credited in the same manner, and that we will on or before the tenth day of the same month, send a cheque of the Prescription Optical Co. Ltd. to each shareholder respectively, representing the difference between the invoice price and the retail sale price." Imperial further guaranteed that the amount paid to each shareholder over a year should aggregate an amount at least equal to $4.50 for each prescription so directed, inclusive of all repair work and whether the prescription accepted was paid in cash or delivered on credit. Thereafter, until March 31, 1946, the doctor-shareholders of Prescription (who varied in number and name from time to time) received no dividends from their shares, but did regularly receive the commissions or payments and the statements provided for in the letter Exhibit 3.

The appellant is a leading ophthalmologist in Vancouver. In 1936 he was invited by Dr. Smith (president for many years of Prescription), and perhaps by Boyaner to become a shareholder in place of a doctor who had recently died, and agreed to do so. Accordingly, one share was transferred to him, and while he expected to pay one dollar therefor, it seems that he paid nothing and did not even receive a share certificate. While he did not see the 1931 agreements between Imperial and Prescription, he was made fully aware of their contents. Thereafter, until March 31, 1946, he regularly received the statements from Imperial, as well as the payments provided for in Exhibit 3, averaging for several years prior to 1946 about $5,000 anually. Such receipts, he states, were reported as part of his taxable income, and income tax paid thereon. Some of the other shareholders received more in commissions than the appellant, and others less.

The *Medical Act* of British Columbia was amended by s. 79 of c. 44 of the Statutes of 1946 (in effect April 11, 1946) and thereafter it became illegal for any member of the College of Physicians and Surgeons of that province to take or receive any remuneration by way of commission, discount, refund or otherwise, from any person who filled a prescription given or issued by such member, and penalties were provided for persons guilty of an offence thereunder. That section clearly applied after April 11, 1946 to commissions or payments such as had been paid by Imperial to the shareholders of Prescription, and Imperial, Boyaner and the shareholders were fully aware of the effect of the amendment.

Following the amendment to the *Medical Act,* the appellant continued to direct prescriptions to Prescription in about the same proportion as he had previously done, i.e., about 50 per cent. of those issued by him; about 15 per cent. were directed to another optical company which provided somewhat faster service, and the remainder were directed to other companies chosen by his patients. The appellant stated that his preference had always been in favour of Prescription as its services were excellent. He states positively that he received no commissions from Imperial or Prescription in respect to referrals made after April 11, 1946.

I turn now to the evidence relating to the transfer in 1947 of the 24 issued shares of Prescription to Standard, a wholly-owned subsidiary of Imperial. The only oral evidence is that of the appellant and it is indeed very limited. While he was a director as well as a shareholder of Prescription, he appears to have taken a relatively minor part in the negotiations with Imperial. He attended only one meeting and was unable to fix its date except that it was in the summer or late summer of 1947. He states that in view of the amendment to the *Medical Act,* the most important thing was to get out of Prescription entirely, preferably by sale of the shares if that could be arranged. Since 1931, Prescription owned no physical assets, all of which had been transferred to Imperial and that company had also operated the business, using the name Prescription. The doctor-shareholders of Prescription, however, had the right to terminate the agreement of 1931 by one week's notice, and had they done so, they would presumably have had the right to resume the

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operation of Prescription (as had been done prior to 1931), using the name of Prescription Optical Co. Ltd.; or they might have disposed of the business by sale.

The one meeting attended by the appellant was held from sixteen to eighteen months after the amendment to the *Medical Act* and while it is clear that the negotiations had previously been carried on by Dr. Smith and a small committee of the shareholders, with Boyaner representing Imperial, there is no evidence as to what took place in such negotiations.

Some fifteen shareholders met with Boyaner at the meeting referred to. The appellant states that it was then agreed as follows:

1. Imperial's offer of $320,000 for all the 24 issued shares in Prescription should be accepted.
2. That only the twenty shareholders then in active practice should receive any part of the compensation.
3. That the total amount of $320,000 should be divided among the twenty participating shareholders in proportion to the number of prescriptions each had sent to Prescription over the last three years; and that as Imperial alone had the records showing the referrals of each doctor, the apportionment should be as Boyaner might determine.
4. That special consideration should be given by Boyaner to doctor-shareholders who had served in the Armed Forces in the recent war.
5. That if any doctor who was entitled to share in the distribution should die or retire from practice, Imperial would pay only one further year's instalment "plus *pro rata* for the number of months practiced since our previous payment".

Dr. McLean stated that Boyaner's first offer was $200,000; that the shareholders asked for $400,000 but that finally the parties compromised at the sum of $320,000. Whether the condition that the payments would terminate in the event of death or retirement from practice formed part of Imperial's original offer, or only of the final offer, does not clearly appear. There was no discussion as to distributing the full amount of $320,000 between the shareholders according to their share holdings (i.e. equally) and Dr. McLean was of the opinion that any such suggestion would have been immediately rejected. Dr. McLean was unable to state why the doctors present had asked for $400,000, except that it was double the amount originally offered and seemed to be good bargaining procedure.

The appellant was of the opinion that it was proper to divide the agreed price among the twenty active shareholders in proportion to the referrals made in the previous three years, as by these referrals they had helped to build up the business of Prescription in varying proportions.

Now if the agreements so arrived at were in fact carried out without amendment or addition, then in view of the appellant's emphatic statement that there was no agreement express or implied that the payments he so received were contingent upon his continuing to send prescriptions to Imperial and/or Standard, the conclusion might possibly be reached that he was doing nothing more than selling his own share at a price to be fixed by Boyaner, payable in annual instalments, but terminable, as stated above, in the event of retirement from practice or death. There is evidence, however, which indicates that the entire matter was not finally settled at the meeting attended by the appellant. That meeting, I think, was probably held on or about June 23, 1947, the date referred to in the Notice of Appeal, and which agrees with the evidence of the accountant, Mr. McIntosh, as being the date of the take-over by Imperial. Exhibit 7 indicates that the shares were registered in the name of Standard on August 4, 1947.

I refer particularly to Exhibit 4, a letter bearing the date November 1, 1947, addressed by Standard to the shareholders of Prescription, which is as follows:

Dear Dr.

This letter is to confirm the sale of your shares in the Prescription Optical Co. Ltd. to ourselves as of April 1st, 1946 on the following basis.

We are purchasing your shares in the Prescription Optical Co. Ltd. for the price of $ on the following terms and subject to following conditions.

10% of the total amount each year.

First payment will be made August 15th, 1947 and each successive payment will be made on August 15th of each year until the complete ten payments are made.

Should you retire from practice or pass away before these ten payments are completed, then we will pay one year's installment plus pro rata for the number of months practised since our previous payment. This final payment will be paid and accepted with the clear understanding that any outstanding balance is automatically cancelled and nothing further is due you or your estate.

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As part of the consideration for the purchase and sale of your shares you have handed to us your agreement under seal of even date, releasing us from any demands, etc., as well as a letter confirming this sale and purchase and adding terms upon which we have agreed.

The appellant acknowledges having received a copy of that letter directed to him and stating his price to be $29,172.52. He agrees that he continued in practice, received the annual payment of 10 per cent. of that amount in each of the taxation years in question and thereafter until the full amount had been paid him. While he recalled that Boyaner had brought him that letter, he could not recall the date but thought it was in 1948. He did not know until then the amount that had been allotted to him and was not aware of the amounts allotted to the other nineteen shareholders until the Enquiry some years later by the Income Tax authorities.

At first, Dr. McLean did not admit that he had seen or signed the two documents referred to in Exhibit 4, but finally, and somewhat reluctantly, admitted that Boyaner had brought two documents for his signature, that he had signed them and given them to Boyaner; and that these were presumably his "agreement under seal of even date herewith releasing us from any demands, etc.", and "a letter confirming this sale and purchase and adding terms upon which we have agreed"—as referred to in Exhibit 4. He was unable to say what was contained in either the letter or the agreement, although he was sure that they contained no undertaking on his part, morally or legally, to continue sending prescriptions to Prescription.

In support of the appellant's case, J. E. McIntosh, a chartered accountant of Vancouver, was called to give opinion evidence as to the value of the shares sold to Standard as of June 23, 1947. He had had some experience in valuing shares of private companies and had access to the books of Prescription for some years prior to and after the sale to Standard or Imperial in June, 1947. In his opinion, they were worth $312,000. He considered that the provisions in the agreement of 1931 between Prescription and Imperial (Exhibit 2), giving Prescription the right to terminate that agreement on one week's notice, conferred on the shareholders of Prescription a valuable right, namely,

the right to again operate Prescription Optical Co. Ltd. as their own concern with all the goodwill that had been established between 1924 and 1947, or to sell it as a going concern.

His report, consisting of five schedules, was filed as Exhibit 22. As shown in Schedule 1, he found that the average net profit for the years 1943 to 1947 was $51,632 and that if income tax had been paid thereon (instead of diverting the whole of it to the doctor-shareholders as was done up to March 31, 1946), the average net profit after taxes would have been $33,561. Schedule 2 is a comparative statement of the operating results of Prescription (as operated by Standard or Imperial) for the years 1948 to 1954, and indicates an average annual net profit before taxes of $52,686, or substantially the same as for the years 1943 to 1947.

His computation of value is found in Schedule 3. He capitalized the annual net profits after taxes for the years 1943 to 1947 of $33,561 at 12½ per cent. or 8 × earnings, resulting in a capitalized value of $268,488. From that he deducted $15,000 as the amount estimated to be necessary for purchase of fixtures and inventory; he then added an interest factor calculated at 5 per cent. to convert the value of the shares payable in cash to a price payable one-tenth down and the balance in nine equal annual instalments without interest ($59,158), arriving at a capitalized value for all shares of $312,646 which he rounded to $312,000.

In his opinion, considering the gross income and the net profits for the years 1943 to 1947, the small amount of capital that would have been required, the stability of the optical business as a whole and the simplicity of the operations involved, a buyer would have been willing to pay $312,000 for all the shares even if he had had no previous experience in that business. He was also of the opinion that it would have been worth even more to a wholesale optical company such as Imperial which would have a continuing and assured outlet for its manufactured products. In addition, he said that the net profits actually realized by the purchaser in the years 1947 to 1954, inclusive, confirmed his estimate of value.

In cross-examination, Mr. McIntosh admitted that he had had no previous experience in valuing shares of an optical company, nor in any transaction such as the present

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one where payments ceased on death or retirement. He was also referred to his evidence before the Income Tax Appeal Board.

> Q. Do you mean to say that a man, any reasonable business man would pay out $300,000 odd in the pious hope that these few people on whom he absolutely had to depend would continue to send him business without any payment?
>
> A. No, sir. I think that any astute and prudent business man would not have bought these shares had he not every reasonable expectation of receiving custom from the very people from whom he was buying the shares. And further, I think that he would have been most prudent, if he had made a purchase on the same basis as Mr. Boyaner was able to do for his people. That is, on a ten-year payment basis, because I think that the sellers would have had more of an interest in continuing to refer business to the operation if they were being paid over a ten-year period, than if they received their cash all at once.
>
> Q. It is the psychological picture you are talking about now?
>
> A. I think it is a very important psychological aspect.

I take that statement to mean that no prudent and reasonable person would have paid $320,000 for the shares if he had only a "hope" that the former doctor-shareholders would continue to send prescriptions to Prescription without any payment therefor; but that such a purchaser would pay that amount only if he had *every reasonable expectation* of having referrals made thereafter by the former doctor-shareholders.

As stated in *Johnston v. M.N.R.*[1], the onus is on the appellant, and the taxpayer must establish the existence of facts or law showing an error in relation to the taxation imposed upon him. In that case, Rand J. said at p. 489:

> Notwithstanding that it is spoken of in section 63(2) as an action ready for trial or hearing, the proceeding is an appeal from the taxation; and since the taxation is on the basis of certain facts and certain provisions of law either those facts or the application of the law is challenged. Every such fact found or assumed by the assessor or the Minister must then be accepted as it was dealt with by these persons unless questioned by the appellant. If the taxpayer here intended to contest the fact that he supported his wife within the meaning of the Rules mentioned he should have raised that issue in his pleading, and the burden would have rested on him as on any appellant to show that the conclusion below was not warranted. For that purpose he might bring evidence before the Court notwithstanding that it had not been placed before the assessor or the Minister, *but the onus was his to demolish the basic fact on which the taxation rested.*

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

After a most careful examination of the evidence, I have come to the conclusion that the appellant has not satisfied the onus cast on him to establish error in fact or in law in the assessments. That decision has been reached mainly because of the failure of the appellant to adduce material evidence which I think was available, which constituted part of the whole transaction and which would have disclosed the true nature of the contract finally entered into with Imperial and/or Standard. In reaching that conclusion, it is quite unnecessary to cast any doubt on the honesty or integrity of the appellant which was admitted by counsel for the respondent. Further, I make no finding that anything done by the appellant could be considered as a breach of the *Medical Act* of the province of British Columbia.

As shown by the Minister's reply to the Notice of Appeal, his main submission was that the annual sums so received by the appellant for the taxation years in question were properly included in the computation of the profit from his business or calling. In the re-assessments in appeal, the Minister assumed

(*a*) that as of June 23rd, 1947, the date referred to in paragraph 5 of the "Statement of Facts", there was due, owing and unpaid by Imperial Optical Company to the Appellant and other shareholders of Prescription Optical Company Limited under and by virtue of the undertaking of Imperial Optical Company referred to in paragraph 3 hereof divers sums of money;

(*b*) that the sum of $29,172.52 referred to in paragraph 6 of the "Statement of Facts" was the sum that the Appellant could expect to receive over a period of ten years by annual instalments of $2,917.25 under and by virtue of an understanding expressed or implied whereby it was understood between the Appellant and Imperial Optical Company, inter alia,

(i) that the sums referred to in subparagraph (*a*) that were due, owing and unpaid to the Appellant should not be paid,

(ii) that the Appellant would transfer his share in Prescription Optical Company Limited to Standard Optical Company Limited, the nominee of Imperial Optical Company,

(iii) that the Appellant should receive from Standard Optical Company Limited on August 15th each year for a period of 10 years from April 1st, 1946, or so long as he should not retire from practice or die, whichever was the shorter, a sum of $2,917.25,

(iv) that the Appellant would continue to encourage his patients to have their prescriptions filled by Prescription Optical Company Limited.

The assumptions referred to in paras. (*a*) and (*b*)(i) were not challenged in any way and must therefore be accepted as facts. They refer to the commissions for referrals which under the agreement of 1931 had accrued to the

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doctor-shareholders between April 11, 1946 and June 23, 1947, and which on the evidence would amount to about $60,000. The assumption in para. (*b*)(ii) is admittedly correct as is also that found in para. (*b*)(iii), with unimportant variations earlier referred to.

The assumption found in para. (*b*)(iv) is of the greatest importance. In the appeal, Dr. McLean was referred to certain evidence given by him before the Tax Appeal Board and also at the Enquiry before Mr. MacLatchy. At the Enquiry he answered certain questions as follows:

Q. What were they getting assuming now, as the evidence shows, that this company had no assets of any kind, had not been in existence for sixteen years, what was the value they were buying that would justify paying you $29,000.00?

A. They were buying goodwill.

Q. What goodwill?

A. Goodwill of the men dispensing glasses.

Q. Which?

A. The goodwill of the man dispensing glasses, the oculist dispensing glasses.

Q. That is your goodwill personally?

A. That is right.

* * *

Q. That is the logical conclusion, and that is what I wanted you to give me, but actually you were being paid for your own goodwill that you would continue to send these prescriptions.

A. Yes, I imagine that is true.

At the Enquiry, he was also questioned regarding the allotment made by Boyaner to Dr. Galbraith who became a shareholder in June, 1946.

Q. But were increased periodically; I am merely trying to get the pattern. Dr. Galbraith had received no money. He had in this period of 1946 a credit considerably smaller than yours, about half of the amount, and he received approximately the same amount you did; do you think that was a proper division?

A. I would accept it as a proper division, yes.

Q. On the basis, I take it, Doctor, that again they were buying Dr. Galbraith's goodwill, that he was going to increase sending in prescriptions?

A. Yes.

Before the Income tax Appeal Board, the appellant admitted having made those answers, but endeavoured to qualify them to some extent, particularly in regard to the nature of the goodwill which gave value to the shares. There he admitted that his statement at the Enquiry, that he was

being paid for his own goodwill that he would continue to send them prescriptions, was true, but added, "They wanted us to send prescriptions, but we didn't have to send prescriptions". He did not attempt, however, before the Board, to qualify his answers at the Enquiry in regard to the allotment to Dr. Galbraith. In this appeal, he admitted having made the above statements at the Enquiry and before the Income Tax Appeal Board, but endeavoured again to qualify them further by saying that they were only partly correct. In reference to the goodwill being sold, he said:

> We feel that the goodwill of the men dispensing glasses was only a part and a minor part of it. The other parts were the goodwill of the public and the patients that you refer. They gave good service, good quality and prices; they were satisfied that the Prescription Optical Company were doing a good job towards the public and towards the doctors.
>
> And we were not paid for our goodwill if we continued to send the prescriptions, we were not being paid for any future purpose in any way. We had no obligation. The thing we were selling was a share, and that share represented goodwill of the patients, the public and the doctors.
>
> They (i.e., the purchasers) hoped we would continue to feel kindly towards them and send prescriptions to them, but at no time was there any compulsion or any agreement or any moral or legal obligation, or any form of obligation to send prescriptions. That is the part I want to emphasize.

Then, in reference to Dr. Galbraith's allotment, he said:

> Dr. Galbraith was paid for the purchase of a share, for the sale of a share which represented his goodwill, the public's goodwill and the patients' goodwill.
>
> The patients that he had sent to the company and the public who were not necessarily patients of his.

I find it difficult to reconcile the obvious inconsistencies between the earlier statements of the appellant and those given at this hearing, although they may possibly be due to the fact that the events occurred in 1947.

I am satisfied in this case that all the details of the transaction have not been presented to the Court. It is undoubtedly true that the transaction involved the sale of the appellant's one share to Standard, but it is equally clear that that was not the only matter agreed to and that other considerations were involved, the nature of which was not disclosed to the Court. I refer to the release and letter mentioned in Exhibit 4 and which were signed by the appellant at the time he received Exhibit 4 and his first payment. If, as stated in Exhibit 4, they formed *part* of the consideration

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for the sale of the appellant's share, the Court is entitled to know their contents and could not without such information come to the conclusion (as the appellant requests) that the *whole* of the consideration was for the transfer of the share. What was the nature of the "release from any demands, etc.?" There is nothing to suggest that the appellant had previously any dealings with Standard which would require a release. Does the release refer to the accumulation in the hands of Imperial of commissions or referrals between April 11, 1946 and June 23, 1947? Again, what were the terms of the letter confirming the sale and purchase "and adding terms upon which we have agreed"?

On these important matters no information whatever is given to the Court except that the appellant, after stating that he was wholly unaware of their contents, did say that they contained no undertaking on his part to send further prescriptions. That, of course, was not the best evidence available. Dr. McLean contented himself by saying that he had made a search in his own papers and could not find them—a result to be expected in view of his statement that he had previously delivered them to Boyaner. Presumably, all twenty shareholders had signed similar documents and given them to Boyaner. The appellant, however, admits that he had made no further effort to secure them or to ascertain their contents from Boyaner or Imperial and he did not require them to produce them to the Court as he could and should have done to complete his case. The Court, in endeavouring to ascertain the true and complete nature of the transaction, must be fully informed by the production of all relevant, material and available documents, and here the burden of producing such information was upon the appellant and has not been satisfied.

Other matters, also, are not satisfactorily explained. In his evidence, Dr. McLean on two occasions stated that when Boyaner brought Exhibit 4 to him, he, the appellant, had handed over a cheque, but nothing was said as to the purpose of that payment. If the terms of the sale were fully agreed upon at the meeting of June 23, 1947, why was the settlement delayed until at least November of that year, and what further negotiations took place during that time which led up to "the new terms upon which we have agreed?" Why was the share sold "as of April 1, 1946" when there is no evidence to suggest that it was so agreed at the

meeting of June 23, 1947? If each shareholder was legally entitled upon a sale of the business to receive one-twenty-fourth of the sale price, why were the estates of three deceased shareholders allotted nothing and why was one doctor who was about to retire also allotted nothing? Was it because they were no longer in practice? Why would six doctors who became shareholders only in 1946 be allotted a total of almost $75,000 (Exhibits A, F and G) and why would one of these (Dr. Galbraith) receive an amount almost comparable to that of the appellant who became a shareholder in 1936, and another receive only about $4,500? If the shares were in fact worth $312,000, as estimated by the witness McIntosh, why would the shareholders consent to an arrangement under which all remaining annual instalments of the purchase price, save one, would be forfeited upon death or retirement from practice?

What happened to the accumulation of commissions or referrals between April 1, 1946 and June 23, 1947, which may have amounted to as much as $65,000 to $70,000? Was Imperial released from its liability to make such payments and if it did so, was that amount part of the purchase price? And if the agreement was fully settled on June 23, 1947, why was not Boyaner called to establish that the allotment of the purchase price between the twenty practicing doctors, as shown by Exhibit A (and in which the amounts allotted vary from a low of $1,795.23 to a high of $54,754.48) was in fact according to the number of prescriptions referred to Prescription by the shareholders in the last three years, with special consideration to doctors who had served in the Armed Forces? There is no evidence on that matter. Why was the sale made to Standard rather than to Imperial, with which latter company the matter was discussed in June, 1947? These matters, which are either wholly unexplained or in which the explanation is unsatisfactory, strongly suggest that after the meeting of June, 1947, further negotiations with Imperial were conducted by Dr. Smith and his committee leading up to the agreement of release and "the letter adding new terms", both as referred to in Exhibit 4.

In view, therefore, of the fact that the appellant has failed to adduce available evidence which was material to a determination of the true and full nature of the transaction entered into, I must find that he has not established

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to my satisfaction that there is error in fact or in law in the re-assessments under appeal. In these circumstances, it is unnecessary to consider the alternative submission of the respondent that the payments received by the appellant were benefits conferred on him by Standard within the meaning of s. 125(2) of the 1948 *Income Tax Act* and of s. 137(2) of the *Income Tax Act*.

Accordingly, the appeal will be dismissed and the re-assessments in appeal affirmed. The respondent is entitled to his costs after taxation.

Judgment accordingly.

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Feb. 20 & 28

Sept. 11

BETWEEN:

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

AND

UNITED AUTO PARTS LIMITED .....RESPONDENT.

Revenue—Income tax—Income Tax Act 1948, S. of C. 1948, c. 52, ss. 11(1)(c), 12(1)(c), 42(6) and 124(12)—The Income Tax Act, R.S.C. 1952, c. 148, ss. 11(1)(c), 12(1)(c), 46(7) and 136(12)—Deductions—Interest on debentures—Validity of assessment—Defect in notice of assessment—Appeal allowed.

Respondent company, a dealer in auto parts, bought and sold them to the general public at a profit and also to companies it controlled. In October, 1946, it borrowed $1,060,000 at 4½% interest from a bank and in December of the same year purchased several companies dealing in auto parts at a cost of $988,029. In December 1947 it issued debentures amounting to $1,000,000 bearing 3½% interest and sold them to its bank which applied most of the proceeds in reduction of the company's bank loan. Respondent claimed a deduction for the interest paid on these debentures which deduction was disallowed by the appellant on the ground that the proceeds were not used to earn income from a business or property under s. 11(1)(c) of the Act but were used to acquire property the income of which was exempt and that s. 12(1)(c) applied. An appeal to the Tax Appeal Board was allowed and from that decision the Minister appeals to this Court. The respondent contends that the proceeds from the debenture issue had no connection with the purchase of shares of subsidiaries because the shares had already been bought and paid for in the previous year. The Minister at the hearing of the appeal from the Tax Appeal Board introduced new evidence which showed that the debentures issued in April, 1947 had been antedated to August 1, 1946. A subsidiary point raised was

that the notice of assessment bore the facsimile signature of a person who was no longer the Deputy Minister of National Revenue for Taxation at the time.

Held: That the appeal must be allowed.

2. That the respondent and its officers treated the debentures in the same manner as if they had been issued in August, 1946, when no bank loan existed and the debenture issue was contemplated when the loan was effected.

3. That the proceeds of the debentures were not used for the purpose of earning income from a business or property within the meaning of s. 11(1)(*c*) of the Act, and respondent was not entitled to deduct the interest payable on the debentures.

4. That any defect that may have existed in the assessment notice was remedied by s. 42(6) now s. 42(7).

APPEAL from the Tax Appeal Board.

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

Lovell C. Carroll, Q.C. and *Paul Boivin, Q.C.* for appellant.

Neil F. Phillips and *Ivan E. Phillips* for respondent.

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

KEARNEY J. now (September 11, 1961) delivered the following judgment:

This is an appeal from a decision of the Income Tax Appeal Board rendered on June 26, 1953[1].

In computing its income tax return for the year 1950, the respondent, on the ground that it represented interest on borrowed money used for the purpose of earning income from its business, claimed as a deduction an amount of $24,500 paid out as interest on serial debentures which it issued in 1947 amounting to one million dollars. By notice of assessment, the appellant disallowed the said deduction, the respondent objected thereto, but on review the assessment was confirmed by the appellant. The Board, in its decision, allowed the appeal and the deduction sought and referred the matter back to the Minister for reassessment accordingly.

On October 31, 1946 the respondent borrowed on call loan from the Bank of Toronto $1,060,000 bearing interest at 4½ per cent and on that date $988,029 thereof was used by the respondent in respect of a purchase, as later described,

[1] 8 Tax A.B.C. 358.

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of all the outstanding shares of several companies which were engaged in a similar business to its own. Debentures amounting to $1,000,000 were issued by the respondent on April 2, 1947 and sold to the same Bank, which applied $988,029 thereof in reduction of and in substitution *pro tanto* of the respondent's outstanding call loan. The connection, if any, between the shares purchased and the proceeds of the debentures to the extent of $988,029 and the consequences which follow in either event constitute the main issues in the present case.

The applicable provisions of the *Income Tax Act*, S.C. 1948, c. 52, are ss. 11(1)(*c*) and 12(1)(*c*), which read as follows:

> 11 (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:
>
> (*c*) an amount paid in the year or payable in respect of the year (depending upon the method regularly followed by the taxpayer in computing his income) pursuant to a legal obligation to pay interest on
>
> (i) borrowed money used for the purpose of earning income from a business or property (other than property the income from which would be exempt), or
>
> (ii) an amount payable for property acquired for the purpose of gaining or producing income therefrom or for the purpose of gaining or producing income from a business (other than property the income from which would be exempt) or a reasonable amount in respect thereof, whichever is the lesser;
>
> 12 (1) In computing income, no deduction shall be made in respect of
>
> (*c*) an outlay or expense to the extent that it may reasonably be regarded as having been made or incurred for the purpose of gaining or producing exempt income or in connection with property the income from which would be exempt.

The parties agreed that the evidence and argument before the Tax Appeal Board should form part of the record, and it was filed as Exhibit 1; and in addition, as not infrequently happens in an appeal such as this, which is in reality a trial *de novo*, the appellant adduced new evidence which was not before the Board.

It appears by the evidence given before the Board that the respondent, as its name implies, is engaged in various facets of the auto parts business. It purchases this type of merchandise from manufacturers and sells it at a profit partly to the general public and partly to such subsidiary companies which it may own or acquire. It likewise derives

income from management fees which it charges to its subsidiaries. Since it supplies the inventory required by its subsidiaries as well as its own, the volume of its purchases is large and it is, consequently, able to obtain discounts or reduced prices from the manufacturers, the larger the volume the larger is the reduction. It does not pass on the benefit of the discounts it receives to its subsidiaries but charges them a set up price approximately equal to the purchase price which these various subsidiaries would have been required to pay had they individually made such purchases themselves.

The new evidence was introduced by the appellant for the purpose of disproving the respondent's contention that the debentures issued in 1947 and subsequent interest paid thereon had no connection with the purchase of the newly acquired shares of the subsidiary companies and that they were part-payment of one continuing transaction. This evidence consisted of Exhibits 2, 3, 4 and 5 comprising extracts from the respondent's books of account which include a copy of its balance sheet and auditors' report for the year 1946, minutes of directors' meetings held in December 1946 and February 1947.

Perhaps the most revealing part of this new evidence is Exhibit 4. It contains a copy of the minutes of a meeting of the directors of the respondent company held on December 27, 1946. There were present all of the three directors of the company and Mr. Charles E. Préfontaine acted as president. Mr. Préfontaine stated to the meeting that he was then the owner of all the capital shares of five companies (previously referred to as subsidiaries), which he offered to sell to the respondent company for $1,115,769, on account of which the respondent had already paid to his exoneration the sum of $1,026,829.

It appears from the evidence taken before the Board that the shares of the five above-mentioned companies were closely held but not by Mr. Préfontaine. So it is clear that Mr. Préfontaine must have acquired four of them with monies supplied by the respondent, which it had borrowed from the Bank. This appears by Exhibit 2 (p. 3), which is

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an extract from the respondent's general ledger entitled: "Account C. E. Préfontaine re Purchase of Shares Affiliated Co's Account", which shows that on October 31, 1946 his account was debited with $988,829.09, which was cancelled by a credit entry for the same amount on the same day.

Minutes also show that in addition Mr. Préfontaine offered to sell all the issued shares of about twenty-five other companies, of which he himself had been the owner for some time and most of which were regional offshoots of the respondent company, for a sum totalling $427,308; and at the same time he offered to subscribe for 28,866 common shares and 5,000 preferred shares of the respondent company for a total amount of $543,077. The directors voted in favour of accepting the two above-mentioned offers, Mr. Préfontaine abstaining. The latter transaction is also reflected on Exhibit 2, p. 3. As a result of the aforesaid transactions, the respondent's investment in shares of subsidiaries was in excess of $1,500,000.

Exhibit 4 also contains a copy of the minutes of the meeting of directors of the respondent company held on the 12th of February 1947, whereat a special borrowing by-law was enacted which, *inter alia,* authorized the directors to borrow money upon the credit of the company and, by trust deed, to create and issue debentures up to an aggregate amount of $1,000,000 at such rate of interest, maturity and redemption as the directors may see fit to approve.

The minutes of a subsequent meeting of directors held on the 17th of February 1947 show that the above-mentioned special by-law has been approved at a meeting of shareholders held on February 15, 1947 and that the directors passed a resolution creating serial debentures not exceeding $1,000,000. A draft trust deed was likewise approved, subject to such changes, additions and variations as may be approved by the president and vice-president of the company prior to the execution thereof, and a trustee appointed. The debentures were to be dated August 1, 1946 and bear interest at 3½ per cent per annum. It appears that subsequently a provision for their redemption, at the rate of $100,000 per year, dating from August 1, 1946, was inserted in the trust deed.

A short time after the above meeting, namely, on April 2, 1947, another meeting of directors was held, an extract from which was filed before the Board as Exhibit 2, which reads in part as follows:

It was resolved:

That the company sell at par to the Bank of Toronto debentures of this company for $1,000,000.00 such debentures bearing interest at the rate of 3½% per annum, secured by a trust deed of hypothec, mortgage and pledge bearing formal date of August 1st 1946, executed by this company in favor of Crown Trust & Guarantee Co. as trustee on the 2nd of April 1947, before Lionel Leroux, notary.

That this company having received from the Bank of Toronto payment in full of the said amount of $1,000,000.00 does hereby authorize the Crown Trust & Guarantee Co. to deliver to the Bank of Toronto such debentures for an amount of $1,000,000.00.

That the President be and is hereby authorized to instruct the Crown Trust & Guarantee Company accordingly.

Page 1 of Exhibit 2, which is an extract from the Company's general ledger dealing with its bank loan, indicates that as of August 31, 1946 the respondent company had no bank loan and that the bank loan of $1,060,000 with which we are concerned was obtained on October 31, 1946. The ledger also shows that on July 31, 1947 the bank loan was reduced by the proceeds of the debenture issue of one million dollars, and there is no doubt that $988,029 of it cancelled a like amount that the respondent had borrowed on call loan to pay for the shares of the subsidiary companies.

The auditors' report for the year ended December 31, 1946 (Ex. 3) brings into that year the debentures issued on April 2, 1947, and they were antedated to August 1, 1946. This million-dollar-debenture issue also appears on the "liability" side of the respondent's balance sheet as of December 31, 1946 (Ex. 3).

In *Canada Safeway Limited* and *The Minister of National Revenue*[1] at page 727, *in fine*, Rand J. observed:

. . . . in the absence of an express statutory allowance, interest payable on capital indebtedness is not deductible as an income expense.

In order to succeed, I think the respondent has a double burden to discharge. It must prove that the interest paid on the debentures issued in 1947 was not an outlay that may be reasonably regarded as having been incurred in connection with property the income from which would be exempt

[1] [1957] S.C.R. 717.

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within the meaning of s. 12(1)(*c*); and even if this is established, it must also prove that it can be said that the proceeds from the debenture issue were used for the purpose of earning income from a property or business within the meaning of s. 11(1)(*c*). It follows that the case, in a large measure, resolves itself into a question of appreciation of the foregoing evidence.

In my opinion, the proof before me indicates that the Company itself and its officers treated the debentures in April 1947 in the same manner as if they had been issued in August 1946, at which time the respondent had no bank loan. There is no suggestion that on $988,029 of the $1,060,000 which the respondent borrowed on October 31, 1946 it paid any other rate of interest than the 3½ per cent as provided by the debentures. It is important to note that, in contrast with the proof made before the Board, the evidence before me shows that C. E. Préfontaine was the owner of the shares of the entire group of subsidiary companies until December 27, 1946, when the directors of the respondent company authorized their purchase, and that the by-law creating the debentures followed some weeks later.

The provisions of s. 12(1)(*c*) with which we need be concerned read:

> No deduction shall be made in respect of an outlay or expense to the extent that it may reasonably be regarded as having been made or incurred .... in connection with property the income from which would be exempt.

The words "in connection with" are very broad terms, and particularly on the strength of the new evidence and in the absence of any contradictory proof, I think it is not unreasonable to conclude, as the appellant has done, that the debenture issue was contemplated when the loan was effected and that the steps which were taken in the interval form part and parcel of one continuing transaction.

Even if one were to accept the respondent's submission that the proceeds from the debenture issue realized in 1947 had no connection with the purchase of shares of subsidiaries because they had already been bought and paid for in the previous year, I do not see how it can be successfully urged by the respondent that such proceeds were used for the purpose of earning income from a business or property within the meaning of s. 11(1)(*c*)(i) so as to entitle the respondent to deduct the interest paid thereon. In such event, I think

the respondent is precluded from claiming that the repayment had any connection with income in the form of management fees and trade discounts which it was already enjoying because of the purchase of the subsidiary companies, and not one tittle of evidence was offered by the respondent to show that the above-mentioned repayment of the loan was used to produce income in some other form. If the respondent were in the borrowing and lending business—which it is not—any transaction involving repayments of loans might be regarded differently.

Counsel for the respondent relied greatly on the case of *Minister of National Revenue* and *People's Thrift and Investment Co.*[1] I think, in some particulars, the facts in the two cases resemble one another, but they are strikingly different in certain vital respects. In the present case, the lapse of time between the original borrowings from the Bank, which were used to pay for the shares, and the subsequent borrowings from the same party through debentures can be counted in terms of months if not weeks. The corresponding lapse of time in the *Thrift* case has to be reckoned in years. Moreover, in the *Thrift* case, the subsequent borrowings were made from other parties than the original lender. Unlike in the present case, where a retroactive effect was given to the later borrowing which, to all intents and purposes, eliminated the first to the same extent as if it had never been made, in the *Thrift* case it was proven that it was impossible to trace back the later borrowings, which were effected in 1949-1951, or connect them with the purchase of shares made in 1945. In the *People's Thrift* case, the taxpayer's stock-in-trade, so to speak, was that of borrowing and lending money.

For the above reasons I think the respondent has failed to establish that it is entitled to deduct the interest payable on the debentures in question, as contemplated by s. 11(1)(*c*)(i).

I mentioned earlier that by its investment in shares of other companies the respondent stood to derive benefits in its business by way of management fees and trade discounts. It was urged on behalf of the appellant that, regardless of what funds were made use of by the respondent to purchase the shares of subsidiaries, the investment was of a capital

[1] [1959] Ex. C.R. 262.

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nature and the management fees and discounts were only an indirect result therefrom; and that what is contemplated in s. 11(1)(*c*) is the employment or use of borrowed funds which directly result in the earning of income. Because of the conclusion I have already reached, I do not think it necessary to deal with this latter issue.

A subsidiary issue of a technical nature was raised which arose in the following admitted circumstances.

The notice of assessment or reassessment dated January 18, 1952 (see Ex. 1) and mailed to the respondent by the Department of National Revenue in the instant case, bore the name of V. W. Scully, Deputy Minister of National Revenue, Taxation Division. At the date in question Mr. Scully was not the Deputy Minister as above described. The respondent submits that the absence of the name in writing of the person in authority renders the notice of no effect and vitiates all subsequent proceedings taken herein. In support of his denial of this contention the appellant invokes section 42(6), now 46(7), and section 124(12), now 136(12), of the *Income Tax Act*, which read as follows:

> s. 42(6) An assessment shall, subject to being varied or vacated on an objection or appeal under this Part and subject to a re-assessment, be deemed to be valid and binding notwithstanding any error, defect or omission therein or in any proceeding under this Act relating thereto.
>
> s. 124(12) Every document purporting to be an order, direction, demand, notice, certificate, requirement, decision or assessment over the name in writing of the Minister, the Deputy Minister of National Revenue for Taxation, or an officer authorized by regulation to exercise powers or perform duties of the Minister under this Act, shall be deemed to be a document signed, made and issued by the Minister, the Deputy Minister or the officer unless it has been called in question by the Minister or by some person acting for him or His Majesty.

Counsel for the respondent, speaking of the error, observed in his argument before the Board:

> I appreciate it probably issued by reason of a clerical mistake, and the clerical mistake is attributable to the stationery which was used by an old administration, and it was not in the public interest that all this stationery should be used up.

It appears Mr. Scully, who, to common knowledge, had held the office of Deputy Minister of National Revenue, Taxation Division, for many years, was at the date in question *functus officio*. Where facsimiles of signatures are extensively used, errors such as the above described are apt to occur. However,

Exhibit 1, which contains the evidence before the Board, shows that the respondent acted upon said notice of assessment and filed an objection to it, whereupon the appellant, on May 29, 1952, notified the respondent that, having considered its objection, he confirmed the said assessment, and at the bottom of this last-mentioned notice the following inscription is found:

> James J. McCann
> Minister of National Revenue
> (signed)
> Per Charles Gavsie
> Deputy Minister of National
> Revenue for Taxation.

It is not suggested that there is any error or defect in the last-mentioned notice, and I consider that any defect which may have existed in the notice complained of was remedied by the concluding lines of s. 42(6). Consequently, I do not think it necessary to discuss the provisions of s. 124(12).

In the course of his argument, counsel for the appellant conceded that the amount of $24,500 which the Minister disallowed was a little larger than was justified by the facts because it should have been based on the relationship between $988,829.09 and $1,060,000. Another factor which should not be overlooked is that by 1950 $300,000 of the principal amount of the debentures had been repaid.

For the above reasons I think the decision *a quo* should be set aside and the appeal maintained; and I would refer the case back to the Minister for the purpose of reassessment by taking into account the factors previously referred to; and should the parties fail to agree in respect of the reduction to be effected, I will allow counsel to again speak to the matter. Under the circumstances, I do not propose to make any order with respect to costs.

Judgment accordingly.

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Jan. 22
Jan. 25

BETWEEN:

ISRAEL GRADER ..... APPELLANT;

AND

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

Revenue—Income—Income tax—Payment for surrender of lease—Whether income or capital receipt—Income Tax Act, R.S.C. 1952, c. 148, ss. 3 and 4.

The appellant in 1948 leased his theatre from January 1, 1949, at a yearly rental of $5,400 under a lease that provided that the lessee should operate it as a moving picture theatre for not less than nine months in each year. By an agreement entered into in June, 1953 the term was extended for five years from January 1, 1954 at a rental of $5,800 per annum with an option to renew for a further five years at a yearly rental of $6,000. The lessee failed to operate the theatre for the stipulated nine months in 1955, and in June, 1956, a new agreement between the parties provided *inter alia* that notwithstanding anything contained in the 1953 lease, the lessee upon the payment of a monthly rental of $600 commencing July 1, 1956, and payable to the end of the term, should be free to close the theatre and would be discharged of all obligations under the lease and that the lessor for the remainder of the term could make such use of the theatre as he saw fit. On September 1, 1956, the lessor leased the theatre to another tenant at a rental of $3,000 per annum subject to an option to purchase at any time during the term of the lease for $38,000. Four months later the tenant vacated the premises and in 1959 the appellant sold the property for $21,000.

In re-assessing the appellant the Minister added to his declared income for the year 1956 the sum of $3,600 and the sum of $7,200 to his declared income for each of the years 1957 and 1958. The taxpayer's appeal from the assessment to the Tax Appeal Board was dismissed. On an appeal from the Board's decision

Held: That the appellant failed to establish that the closing of the theatre for longer than permitted or that the cancellation of the lease (assuming it took place), caused the property to depreciate and the appellant to suffer a loss when he came to dispose of it.

2. That the thirty monthly instalments of $600 each paid the appellant should be regarded as rental received, or payments in lieu of rental, or in the nature of casual profit derived from a property, and constituted income rather than amounts received on capital account. *Minister of National Revenue v. Farb Investments Ltd.* [1958] Ex. C.R. 113 at 119 followed. *Van Den Bergh Ltd. v. Clark* [1935] A.C. 431 and *Sabine (H.M. Inspector of Taxes) v. Lookers Ltd.* (1958) 38 T.C. 120 distinguished.

APPEAL from a decision of the Tax Appeal Board[1].

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

[1] (1961) 26 Tax A.B.C. 150; 15 D.T.C. 157.

W. D. Goodman for appellant.

G. W. Ainslie for respondent.

KEARNEY J. now (January 25, 1962) delivered the following judgment:

This case concerns an appeal from a decision of the Tax Appeal Board[1] delivered on March 3, 1961 which affirmed three assessments levied by the respondent in respect of the appellant's income tax for the taxation years 1956, 1957 and 1958.

The parties admit the accuracy of the following particulars concerning the said assessments: By two assessments dated July 16, 1958 the respondent reassessed the appellant by adding $3,600 to his declared income for the taxation year 1956 and by adding $7,200 to his declared income for the taxation year 1957 and by assessment dated August 10, 1959 by adding a like amount of $7,200 to his declared income for the taxation year 1958. The appellant duly objected to the said reassessments but the respondent on reconsideration affirmed them and so advised the appellant by notice dated the 20th day of November 1959.

The said amounts of $3,600, $7,200 and $7,200, totalling $18,000, were received by the appellant in the years 1956, 1957 and 1958 respectively from United Century Theatres Limited (hereinafter referred to as "United Century") pursuant to an agreement dated June 26, 1956, and here the parties part company.

Briefly, it is claimed for the appellant that in the particular circumstances the sums in question were payments on account of capital and not taxable, and for the respondent it is said they were receipts on revenue account and taxable accordingly.

The main facts of the case are as follows. The appellant until 1958 was the owner of two-storey premises situated on the south side of King street in the city of Welland, Ontario, consisting of a moving picture theatre, with equipment, on the ground floor and two apartments on the upper floor. By indenture dated November 25, 1948 filed as Exhibit 1, the appellant leased to United Century the theatre portion of the said premises, together with the apartment, fixtures and other equipment, for use as a moving picture theatre, at a rental of $5,400 per annum payable

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$450 in advance on the first day of January 1949 and a like payment in each succeeding month. In view of subsequent events, it is important to note that the aforementioned indenture contained the following provision:

> The lessee covenants and agrees that it will operate such demised premises as a moving picture theatre for not less than nine months in each calendar year.

By indenture dated December 21, 1953, filed as Exhibit 2, the parties extended the term of the above-mentioned lease for an additional period of five years commencing January 1, 1954 and terminating on the 31st of December 1958, at a rental of $5,800 per annum payable in equal monthly instalments in advance. The last-mentioned lease also gave to United Century the option to renew the said lease for a further period of five years at a rental of $6,000 per annum payable by monthly instalments in advance, and provided that all the other terms and conditions of Exhibit 1 shall remain in full force and effect.

While Exhibit 2 had still two years and a half to run, the parties entered into a new indenture dated June 26, 1956, filed as Exhibit 4. This last-mentioned indenture, although it covers less than two pages, is important because it gave rise to the assessments in dispute and I think it should be set out at length:

> Whereas by a certain lease dated the 21st day of December 1953 (hereinafter called the Lease) made between the parties hereto the Lessor demised and leased the premises known as The Community Theatre in the City of Welland in the County of Welland to the Lessee for a term expiring on the 31st day of December 1958, subject to the rent therein reserved and to observance and performance of the covenants and agreements therein contained, all as therein more particularly set forth.
>
> And Whereas under the said Lease it was provided, *inter alia*, that the Lessee would operate the said Community Theatre for at least eleven months in every year.*
>
> And Whereas the Lessee wishes to close the said theatre and the parties hereto have agreed to enter into these presents.
>
> Now Therefore This Indenture Witnesseth that in consideration of the premises and of the agreements herein contained and of other good and valuable consideration the parties hereto mutually covenant and agree as follows:
>
> 1. The Lessor agrees with the Lessee that, notwithstanding anything contained in the hereinbefore in part recited Lease, the Lessee shall be at liberty to close the said Community Theatre and to cease operating the same as a theatre.
>
> *Although unable to explain how the error occurred, the parties agree that the word "eleven" should read "nine".

2. The Lessee agrees with the Lessor that, commencing on the first day of July, 1956, and for the balance of the term of the said lease, the Lessee shall pay to the Lessor a rental of $600 per month in advance on the first day of each month, instead of the present rental set out in the said Lease.

3. It is expressly understood and agreed that, except as to the payment of the increased rental mentioned in the next preceding paragraph 2 hereof, the Lessee shall be relieved and discharged of and from the observance and performance by it of all the terms, covenants, conditions and agreements set forth in the said Lease, including without limiting the generality of the foregoing the obligation to operate the theatre, to repair, to supply heat and to pay insurance premiums or any other sums payable under the said Lease.

4. It is further understood and agreed that, during the remainder of the term of the said Lease, the Lessor may make such use of the said premises as he may deem fit.

5. It is further understood and agreed that all equipment and fixtures and all other contents of the premises now become the property of the Lessor; and that the Lessor may without limiting the generality of Paragraph 4 occupy the premises or rent the premises from the 1st of July, 1956, during the remainder of the said term and that the Lessee shall not thereby be relieved of its obligation to pay the rental hereinbefore stated, and further that the Lessee shall not disturb the possession of the Lessor or anyone claiming under him.

6. This indenture shall extend to and enure to the benefit of the parties hereto and their respective heirs, executors, administrators, successors and assigns.

In Witness Whereof the Lessor has hereunto set his hand and seal and the Lessee has hereunto affixed its corporate seal under the hands of its proper officers duly authorized in that behalf.

Two witnesses, the appellant and Francis P. Sorrentino, were called on behalf of the appellant; no evidence was adduced on behalf of the respondent.

The appellant, in addition to producing the above exhibits, testified that he derives his income from different businesses, Grakor Specialty, an auto parts business, and Selbest Specialty, dispensers of pet food. Apart from the income he derives from the property leased to United Century he also derives income from two stores in Welland as well as from a one-third interest which he has in an apartment house in Toronto.

The appellant stated that in 1955 United Century failed to keep the theatre open for nine months as provided in Exhibit 1. He also expressed the view that because United

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Century owned two other moving picture theatres in Welland, in order not to draw away patronage from these other two theatres, it did not put forward its best efforts with respect to the operation of his theatre.

Subsequently the appellant had discussions with a Mr. Taylor, representing United Century, who, according to the witness, tried to induce Mr. Grader to not insist on the non-closing clause. The witness also stated that if a sum of money were paid for cancellation of the lease he would be disposed to sell the property at a lesser price than otherwise would be the case.

He listed the leased property for sale at an asking price of $55,000 to $57,000, but the best offer made was $30,000, which he received through Mr. Francis P. Sorrentino, real estate broker.

As was his privilege so to do, by indenture dated August 8, 1956 the appellant leased the theatre to Ralph Biamonte of the city of Niagara Falls for a period of one year commencing September 1, 1956 at a rental of $3,000 per annum payable in monthly instalments of $250 each. This indenture does not contain any clause requiring the lessee to maintain the theatre open for any specified period and it contained an option in favour of the lessee to purchase the theatre building and land for $38,000 at any time during the term of the lease, the whole as appears by reference to Exhibit 5.

The witness stated originally that Mr. Biamonte failed to continue to pay the rent after three months, though he continued to operate the theatre for a further month, but could not make a go of it and vacated the premises. Upon being recalled at my instance in order to clear up some ambiguity in his testimony, the witness stated that Mr. Biamonte was unable to procure suitable pictures for the theatre and that after endeavouring to operate it from four to six months he gave up the venture. The witness did not testify as to what was done with the theatre after Mr. Biamonte had vacated it, beyond stating that the property was finally sold for $21,000 in 1958.

Mr. Sorrentino stated that he had been engaged in the sale of commercial real estate in Welland since 1946 and that he knew market values in that city. Although he was unable to secure a better offer than $30,000 for the property, he gave it as his opinion that if it were operating and

repaired it should fetch $55,000. He added that it was located on a secondary street, that B-class pictures had been shown in the theatre and he had observed that during performances the theatre was usually half to three quarters empty. On cross-examination the witness admitted that he had no experience in connection with the sale of theatres and had no financial interest in any theatre companies. He agreed, however, that in connection with theatres goodwill is the most important thing and that he had never attempted to appraise the goodwill of the appellant's theatre. On re-examination he stated that he thought the effect of having allowed the theatre to be closed was detrimental.

In support of the submission that the receipt by the appellant of the $18,000 referred to in paragraph 2 of Exhibit 4 constituted a payment on account of capital his counsel made the following submissions:

(1) That a careful reading of the agreement of June 26, 1956, Exhibit 4, reveals that the sum of money stipulated in the agreement was not paid as rent, notwithstanding the terminology used, but as compensation for the cancellation of the lease.

(2) That it was compensation for a capital loss which it was anticipated that Mr. Grader would suffer when he came to resell the property, by reason of the fact that the theatre was closed.

(3) That Mr. Grader held the leased property as an investment for the purpose of receiving rental income and this theatre did not form part of any business which he carried on.

(4) That in these circumstances the sum which he received was a capital receipt, being compensation for the capital loss which he was expected to suffer and which he did in fact suffer.

It was submitted by counsel for the respondent that the agreement of January 26, 1956 did not operate as an express surrender to the landlord of the term vested in the tenant under the demise and that the amount received thereunder

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by the appellant could not be regarded as anything but rent; and alternatively, that, even if it were found that such surrender occurred, the received amounts in question were casual profits from a property and income from a business within the meaning of ss. 3 and 4 of the Act.

Because of the conclusion which I have reached on the assumption that a complete and effective surrender of the property had occurred, I do not think it necessary to inquire into or to deal with the submission that no complete surrender had occurred.

Usually, to determine whether a receipt of money falls within a category of income or capital is by no means an easy task and often much depends on the particular circumstances of each case.

In Exhibit 4 the monthly payments of $600 are variously specified as "rental" instead of "present rental" and as "increased rental", and since it bears the signature of the appellant, I think, in the circumstances, it falls in the category of evidence against the signatory's own interest. In addition, it is incumbent on the suppliant to show conclusively that on the facts the assessment in question is unjustified.

Although it is lacking in precision, I consider the appellant's evidence established that during the year 1955 the leased theatre did not remain open for the full nine months as required by Exhibit 4. I do not think, however, that it has been established that the fact that the theatre remained closed longer than permitted, or the cancellation of the lease (assuming that it took place) caused the appellant to suffer a loss when he came to dispose of it.

In my opinion no satisfactory proof was made of the market value of the theatre prior to and following the closing complained of. The so-called expert evidence given by Mr. Sorrentino was unconvincing because of his limited efforts and qualifications. He made no attempt to ascertain what the trend was in respect to the saleability of moving picture theatres and whether or not the appellant's experience of not being able to secure a satisfactory price for his theatre was not the common experience of others in the same line of business and attributable to other causes, such as the increasing adverse effect of television and other entertainment media on the picture house industry. The fact that the

appellant was offered $30,000 for the theatre in 1956 but that two years later the best price he could obtain was $21,000 is, I think, some indication of a downward trend in the value of moving picture houses.

Furthermore, the evidence shows the leased theatre remained open during four to six months while it was being operated by Mr. Biamonte, but it failed to attract audiences and Mr. Biamonte could not make enough money to pay his rent; and as evidenced by the Biamonte lease, the appellant, within a matter of months, had reduced the asking price for his property from $55,000 to $38,000.

Mr. Sorrentino testified that what the leased premises lacked was packed houses; yet, no proof was made that other picture houses were not suffering from the same complaint.

I cannot accept the submission of counsel for the appellant that it was sufficient for the appellant to allege or consider that the depressed value of his property was due to the failure of United Century to keep the theatre open in 1955 as was their duty.

Turning again to the evidence of Mr. Grader, I was unfavourably impressed by his otherwise unsupported statement to the effect that he considered the United Century had deliberately kept down the attendance at the leased premises in order to attract greater audiences to the two other moving picture houses owned by that company, particularly when it is in evidence that the United Century had occupied the leased premises for seven or eight years and there is no evidence that any similar complaint was ever made during that period.

I am disposed to the view that regardless of whether the United Century had continued to occupy the leased premises it would not have enabled the appellant to procure a higher price for his property when he sold it in 1958.

Counsel for the appellant referred to *Van Den Bergh Ltd. v. Clark*[1] wherein an English company and a Dutch company which were trading rivals in the manufacture of margarine entered into an agreement to share profits and losses in the proportion which on an average of five years the profits of the rival tradings in margarine bore to each other. Years later disputes arose and the Dutch company paid the

[1] [1935] A.C. 431.

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English company a sum of £450,000 as damages, but the parties did not specify the cause of action in which the damages were paid and it was held that this sum was in the nature of a capital asset and not an income receipt.

Counsel for the appellant also referred to *Sabine (H.M. Inspector of Taxes) v. Lookers Ltd.*[1] wherein it was held that the compensation paid for the variation in the continuity clause of an agreement, which weakened the whole of the profit-making structure of the company suffering such variation was a capital receipt.

The transactions in the above-mentioned cases were extraordinary commercial contracts and the relationship and responsibilities of the parties were, I think, far removed from those arising, as in the present instance, from an ordinary contract of lease and hire of property.

No two cases are exactly alike, but I think a marked similarity exists between the facts in the present case and those which arose in *Minister of National Revenue v. Farb Investments*[2], notwithstanding that in the *Farb* case, instead of a single lease, a lease and a sub-lease were involved. I am also of the opinion that the reasoning set out in the dictum of Cameron J. which is reported at page 119 is apposite in the present case; it reads:

> I may add, however, that quite apart from the above considerations, I would have been inclined to the view that the sum received was not a capital receipt. The question to be decided is not whether in some senses or in some contexts such payment might be called a "capital payment", but whether within the meaning of ss. 3 and 4 of The Income Tax Act, it is the profit arising from the business or property of the respondent. It is not necessary to reach any final conclusion on the matter, but I would point out that the cancellation of the old lease and the giving of a new lease to Imperial Oil in no sense affected the profit-making apparatus of the respondent and its capital structure remained precisely the same as it had previously been.

I think, taking into account all the circumstances of the case and the evidence before me, that the thirty monthly instalments of $600 each paid to the appellant should be regarded in his hands as rental received, or payments in lieu of rental, or in the nature of casual profit derived from a property, and constituted income rather than amounts received on capital account.

[1] (1958) 38 T.C. 120.

[2] [1959] Ex. C.R. 113.

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For the above reasons the appeal must be dismissed. The respondent will be entitled to his costs.

Judgment accordingly.

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BETWEEN:

WALSH ADVERTISING COMPANY LIMITED ..... SUPPLIANT;

AND

HER MAJESTY THE QUEEN ..... RESPONDENT.

Crown—Petition of Right—Claim against Crown for services rendered in connection with sale of securities—Bank of Canada Act, R.S.C. 1952, c. 13, s. 20—Financial Administration Act, R.S.C. 1952, c. 116, Part IV, ss. 39, 41, 42 and 43—Minister not competent to contract—Necessity of Order in Council—No liability on quasi contract—Recovery allowed on quantum meruit basis—Comptroller's certificate.

Suppliant brings its petition of right to recover from the Crown the sum of $60,000 for breach of an alleged contract in 1957. It claimed to have been requested in December, 1956 and in January, 1957 to prepare advertising material, arrange television programmes and generally advertise the government's 1957 campaign for sale of Canada Savings Bonds. It alleged that it had been engaged by the Bank of Canada to perform such services in a previous bond sales campaign and that such arrangement entitled it to consider it would act likewise for the 1957 sales campaign but that its contract was terminated by the Minister of Finance on July 10, 1957, after certain expenses had been incurred and considerable work done in preparation for the campaign.

Respondent contends, *inter alia,* that there was no binding contract entered into between the suppliant and the Crown and that the suppliant had rendered the services in question in the hope of getting a contract.

Held: That there was no binding contract between the suppliant and the Crown at the time of the alleged breach in July, 1957.

2. That by virtue of the *Financial Administration Act,* R.S.C. 1952, c. 116, neither the Minister nor any one acting on his instructions was authorized to enter into a contract on behalf of the Crown relating to the borrowing of money or the issue or sale of securities relating thereto without Parliamentary authority to borrow the money and an Order in Council authorizing the Minister to enter into such a contract.

3. That neither in December, 1956 nor in January, 1957 nor at any time subsequently up to July 10, 1957 when its services were dispensed with was there any such Order in Council authorizing the alleged contract.

4. That since the Crown subsequent to July 10, 1957 had adopted some of the results of the services rendered by the suppliant and used them in the campaign later authorized and conducted it was bound to compensate suppliant on a *quantum meruit* basis.

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5. That s. 39 of the *Financial Administration Act* provides no defence to such a claim as herein presented since that provision applies only in respect of contracts and affords no answers to claims not founded on a contract.

PETITION OF RIGHT to recover from the Crown damages for breach of contract.

The action was tried before the Honourable Mr. Justice Thurlow at Toronto.

The Honourable R. L. Kellock, Q.C. and *D. J. Wright* for suppliant.

W. R. Jackett, Q.C., W. G. Gray, Q.C. and *S. Samuels* for respondent.

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

THURLOW J. now (October 23, 1962) delivered the following judgment:

By the petition of right herein, the suppliant seeks to recover for services rendered and moneys expended pursuant to a contract alleged to have been made in or about November, 1956, whereby the suppliant was employed by the Crown to prepare advertising material, to arrange television programs, and generally to prepare, schedule and place the advertising for the Government's 1957 campaign for the sale of Canada Savings Bonds.

The suppliant alleges that its employment to render these services was summarily terminated after the bulk of the work had been carried out and that it was deprived of the opportunity of recovering the remuneration to which it was entitled under the contract of employment.

The story unfolded in the evidence begins with the following letter, written to the suppliant by the Minister of Finance on June 18, 1955:

> You will have learned from Mr. W. G. Abel that I have decided to continue the advertising accounts in this Department on the same basis throughout this calendar year. I hope he has also told you that I stated to him that at the end of the year there will be a change in your favour.

To this, the suppliant replied on June 21, 1955, as follows:

> This will acknowledge receipt of your letter of June 18th, 1955, in which you inform us that you have decided to continue the advertising accounts in your Department on the same basis throughout this calendar year.
>
> Col. Abel has told us that you stated to him that at the end of the year there will be a change in our favour. . .

We very much appreciate receiving your confirmation of Col. Abel's message to us.

We are looking forward to serving you and your Department, and can assure you that your advertising and public relations problems will receive the best and most conscientious attention of our organization.

At that time, Mr. Abel was vice-president of the suppliant company. He died some time before the trial of the petition.

The next event following the exchange of the letters occurred in May or June of 1956, when several members of the suppliant's staff met with officials of the Bank of Canada in Ottawa and a deputy governor of the Bank outlined certain areas of responsibility which the suppliant was to assume in connection with the promotion of the sale of the eleventh series of Canada Savings Bonds. Thereafter, until the conclusion of the sales campaign in November of the same year, the suppliant arranged for and provided advertising material which was used in the campaign and also arranged for space for such advertising in newspapers and other publications and for television broadcasting time. For the services so rendered the suppliant received payment through a discount or commission allowed to it by the publishers and other parties with whom contracts were arranged. The practice generally followed by these parties was to charge the suppliant or its client for the space, time or services rendered at a gross rate and to pay or allow as a commission to the suppliant on settlement of the account a discount of 15 per cent of the gross amount, with in some cases an additional two per cent for prompt settlement. Where a party in his account charged at a net rate, the suppliant would add its commission on its own invoice for that particular account to its client. This method of realizing payment for advertising agency services was common in the business, there was no secrecy about it, and there is no reason to think that it was not known and accepted by the officials of the Bank of Canada, from whom the suppliant received its instructions, as the basis and manner upon and by which the suppliant was to obtain payment for its services.

Earlier in the year 1956, another advertising agency, at the request of the Bank of Canada, had rendered certain services in developing advertising material for use in the eleventh series Canada Savings Bonds sales campaign, and some time after the suppliant received its instructions it was

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requested by the Bank to pay an account rendered by that agency for its services. The suppliant did this and was reimbursed by the Bank.

To put on a bond sales campaign of the sort that had taken place in 1956 and earlier years involved advertising by a variety of means and on a considerable scale. It entailed among other things the creating of written or printed advertising material, including art work therefor for use in advertisements in newspapers and other publications and in posters and circulars of various kinds, the creation and production of advertising commercials for radio and television programs, the creation, production and distribution of theatre newsclips and the arranging for the publication of the material across Canada at the appropriate time or times. It also entailed work or services of various kinds by many different persons. Needless to say, if all these things were to be done organization, thought and preparatory work could not very well be left to the last minute before a campaign was to be held.

On January 9, 1957, shortly after the conclusion of the eleventh Canada Savings Bond sales campaign, a meeting was held at the request of the Bank of Canada at the suppliant's Toronto office between members of its staff and an official of the Bank "to discuss with him the place of television in the 1957 Canada Savings Bond campaign, on the assumption that there would be a twelfth series of bonds." When requesting this meeting, the Bank had asked the suppliant to consider certain ideas for television advertising for such a campaign, which the suppliant did at a meeting of its staff on or about January 7, 1957, and at the meeting on January 9 these ideas were discussed and the suppliant was asked to undertake a number of particular preliminary tasks in connection with advertising for a twelfth series of Canada Savings Bonds. The suppliant carried out these instructions, as well as many further instructions received from time to time from the Bank both by mail and at ten further meetings held between members of the suppliant's staff and officials of the Bank between that time and June 14, 1957. In so doing, a great deal of time and effort was expended by members of the suppliant's staff and expense was incurred by the suppliant for travelling by members of its staff between Toronto and Ottawa, for telephone calls, for art work for the proposed advertisements, and for the production of

material for films of newsclips and TV commercials. These efforts on the part of the suppliant resulted in the production of some 196 or more pieces of original roughs and preliminary development material for a 1957 Canada Savings Bond campaign. In addition, the suppliant arranged for TV network time for four 90-minute programs and for the services of certain persons to take part in the advertising portions of them and presented estimates of the cost of the proposed advertising campaign, all as requested by the Bank.

No twelfth series Canada Savings Bond campaign had, however, been authorized by the Governor in Council when, on July 10, 1957, the Minister of Finance wrote to Mr. Abel as follows:

> I wish to advise you that the Government has decided to change its advertising agencies in connection with the sale of Canada Savings Bonds. In terminating our relations, I wish to thank you for the services you have rendered the Department of Finance.

This letter was answered on the following day by the manager of the suppliant's Toronto office, who pointed out that a substantial portion of the work of preparing for and organizing advertising for a twelfth series Canada Savings Bond campaign had already been completed and that the advertising agencies derived their remuneration in the form of a 15 per cent commission from newspapers and other advertising media and that he assumed that the suppliant would continue to serve the Department of Finance until the end of the calendar year. The Minister, however, replied on July 12, 1957 that:

> In writing to you on the 10th instant, I did not intend to convey the impression that your firm would continue to serve this Department until the end of this calendar year. Other arrangements have been made for handling the work in connection with the 1957 Canada Savings Bond Campaign, and McKim Advertising Agency Limited will arrange to take over from your firm now.

Subsequently, on August 10, 1957, on the recommendation of the Minister of Finance, an order in council was passed, authorizing the issue and sale of Canada Savings Bonds, series twelve, and in the course of the advertising and sales campaign which ensued some of the suggestions and ideas which originated with or were developed by members of the suppliant's staff and which had been communicated by the suppliant to the Bank of Canada were

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used. Some, if not all, of the TV network time for which the suppliant had arranged was also used, personnel for whose services the suppliant had negotiated appeared on the programs, and a filmed commercial on which the suppliant had devoted time and incurred expense was also used. The suppliant has, however, received no payment for its services and is out of pocket to the extent of $9,873.82 for expenses which it incurred in having the advertising material prepared.

At all material times the Bank of Canada, which by s. 20 of the *Bank of Canada Act*, R.S.C. 1952, c. 13 is required to act as fiscal agent of the Government of Canada without charge and, if and when required by the Minister of Finance, to act as agent of the Government of Canada "in the payment of interest and principal and generally in respect of the management of the public debt of Canada," was in possession of a letter from the Minister of Finance to the Governor of the Bank, dated June 19, 1946, in the following form:

> I have your letter of June 13th with reference to arrangements to be made between the Government and the Bank of Canada in connection with loan flotations.
>
> The Bank of Canada is hereby authorized to make arrangements for and to conduct in the name of the Minister of Finance public loan operations in Canada designed:
>
> (a) to provide facilities to the public for the continuation of systematic savings and investment in such issues of Dominion of Canada obligations as may from time to time be authorized therefor;
>
> (b) to provide funds through channels normally used in the marketing of securities in Canada, to meet the borrowing requirements of the Government of Canada.
>
> In discharging these responsibilities, the Bank of Canada may, with the approval of the Minister of Finance, form a Committee, or other organization, for the furtherance of such operations and also enter into such arrangements and commitments on behalf of the Minister of Finance as may be necessary, subject to the following provisions:
>
> (1) Any basis for the payment of fees, commissions or other remuneration to banks, trust and loan companies, other financial institutions, authorized dealers and salesmen performing services in connection with any such operations for the sale of public issues of Dominion obligations shall be recommended to the Minister of Finance by Bank of Canada and shall upon approval by the Governor General in Council be the authorized basis upon which such fees, commission or other remuneration shall be determined.
>
> (2) Expenses which are incurred in the promotion of the sale of new Government issues and which are properly chargeable against Loan Flotation Charges shall be subject to the approval of the Minister

of Finance given by means of approving in advance a budget covering operations relating to a specific expenditure, and shall be paid by the Government out of unallotted monies in the Consolidated Revenue Fund.

This arrangement appears to have been followed in earlier Canada Savings Bonds campaigns and in the twelfth series campaign as well, and it was not suggested that any commitment incurred in earlier years by the Bank had ever been repudiated, but the authorization of the Bank by the Minister to make commitments is not shown to have been approved by the Governor in Council in any year or for any Canada Savings Bond campaign.

The suppliant's case, as put forward at the trial, was that it was retained either generally or alternatively in connection with the promotion of the sale of Canada Savings Bonds, series twelve, as the Crown's advertising agent, in which capacity it was to produce and develop ideas for advertising and to act as agent for the Crown in making contracts with publishers and others relating thereto, for which services it was to be permitted to place advertising and recover remuneration in the form of discounts or commissions from the publishers and others with whom contracts might be arranged, that it carried out the work requested by the Bank of Canada (which was authorized by the Minister's letter of June 19, 1946 to enter into such arrangements and commitments on behalf of the Minister as might be necessary to carry out its responsibilities for arranging and conducting public loan operations), all of which work was necessary for that purpose, and was entitled to place a particular portion of the advertising for the twelfth series Canada Savings Bond campaign if such a campaign should be authorized and a budget for such advertising approved (both of which events in fact occurred) and to recover remuneration for its services in the way which was customary in its type of business, that the Crown wrongfully broke this contract in July, 1957, by summarily discharging the suppliant as its agent and thereby prevented the suppliant from completing its work and recovering its remuneration and that the suppliant is accordingly entitled to damages equal to the $60,000 or thereabouts which it would have been paid for commissions and disbursements if it had been allowed to complete the work and place the advertising.

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Counsel for the Crown, on the other hand, besides raising a number of other defences, submitted that the suppliant rendered the services in question not in performance of any existing contract with the Crown, but merely in the hope of being awarded a contract for advertising for such a campaign, if held.

In the circumstances disclosed by the evidence, I would infer that the suppliant rendered its services and incurred expenses and commitments in connection with the twelfth series Canada Savings Bonds in the expectation that it would be remunerated by being allowed to place the advertising for the campaign and to receive the commissions in accordance with the practice prevailing in that business, that without such expectation the suppliant would not have rendered the services or incurred the expense or made the commitments and that the Minister and the Bank were aware of this. There is no reason to think that these extensive services were rendered gratuitously, and I would reject the submission that they were rendered by the suppliant purely in the hope and expectation of being awarded a contract for advertising if a bond sales campaign should be held. In the previous year, the services of an advertising agency had been dispensed with prior to the authorization of the eleventh series bonds, but after the agency had done substantial work in preparation for the sales campaign, and the agency had been paid for the services which it had rendered, and I see no reason to doubt that it was contemplated by all parties concerned, when the suppliant was requested to render services in preparation for a twelfth series Canada Savings Bond campaign, that the suppliant would be similarly compensated for what it had done if, by any chance, its services should be dispensed with prior to the completion of the campaign. In view of what had happened in the previous year, I should have thought that it was part of the understanding between the parties that the Minister was to be entitled to dispense with the suppliant's services at any time if he saw fit to do so, in which event the suppliant was to be paid for the services which it had rendered up to that time. However, it is unnecessary to decide whether or not this was a term of the arrangement, for if the arrangement was binding on the Crown the suppliant, having been summarily discharged before the campaign was held, would, in my opinion, be entitled to damages for the breach of its

contract if the contract was to last for the entire campaign or, alternatively, to recover remuneration for the services which it rendered if it was a term of the contract that the Minister might dispense with the suppliant's services at any time prior to the completion of the campaign. In either case, however, the right to recover depends on whether or not the understanding was binding on the Crown.

On this question, a number of contentions were made on behalf of the Crown, but in view of the conclusion which I have reached on one of them it will be unnecessary to deal with the others. The submission in question was based on the provisions of Part IV of the *Financial Administration Act*, R.S.C. 1952, c. 116, ss. 41, 42, and 43 of which were as follows:

41. No money shall be bororwed or security issued by or on behalf of Her Majesty without the authority of Parliament.

42. Where authority is conferred by Parliament to borrow money on behalf of Her Majesty, the Governor in Council, subject to the Act authorizing the borrowing, may authorize the Minister

(*a*) to borrow the money by the issue and sale of securities in such form, for such separate sums, at such rate of interest and upon such other terms and conditions as the Governor in Council may approve, and

(*b*) to enter into such contracts or agreements relating to the borrowing of the money or the issue or sale of securities relating thereto on such terms and conditions as the Governor in Council may approve.

43. The Governor in Council may authorize the Minister to borrow such sums of money as are required for the payment of any securities that were issued under the authority of Parliament, other than section 44, and are maturing or have been called for redemption.

The Crown's submission was that the alleged contract was one relating to the sale of securities within the meaning of s. 42(*b*), that in December, 1956 or January, 1957, when the alleged contract was made, (1) Parliament had not authorized the borrowing of money, and (2) the Governor in Council had not authorized the Minister of Finance to enter into the alleged contract, and that it was therefore not binding upon the Crown.

In my opinion, the second portion of this submission is well founded. It appears to be established as a general proposition that a Minister of the Crown has no authority to enter into contracts on behalf of the Crown unless he has

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been authorized by a statute or by order in council so to do. See *Drew v. The Queen*[1], where the President of this Court said:

> It is an established rule that a contract which involves the provision of funds by Parliament requires, if it is to possess legal validity, that Parliament should have authorized it, either directly or under the provisions of a statute: *vide Mackay v. Attorney General for British Columbia,* (1922) 1 A.C. 457 at 461. And it is an elementary principle that a Minister cannot bind the Crown unless authorized by order in council or by statute: *vide The Quebec Skating Club v. The Queen,* (1893) 3 Ex. C.R. 387; *The King v. McCarthy,* (1919) 18 Ex. C.R. 410 at 414; and *The King v. Vancouver Lumber Co.,* (1920) 50 D.L.R. 6.

In *The King v. McCarthy*[2], Audette J. put the point thus at p. 414:

> Moreover, there is the important question as to whether the Minister of Public Works could under the circumstances, and without valid authority, bind the Crown. Unless authorized by order in council or by statute, a Minister of the Crown cannot bind his Government. The Minister of Public Works, in the matter in question, has obviously no power to enter into such an agreement as set forth in Exhibit No. 24, without proper authority, and without the same he cannot bind the Crown in that respect. The question is so elementary that I shall confine myself in that respect to citing a few cases establishing that proposition, although the authorities are very numerous: *Quebec Skating Club v. The Queen,* (1893), 3 Can. Ex. 387; *Jacques-Cartier Bank v. The Queen,* (1895), 25 Can. S.C.R. 84; and *The King v. The Vancouver Lumber Company,* (1914), 17 Can. Ex. 329, 41 D.L.R. 617, affirmed on appeal to the Supreme Court of Canada on the 4th December, 1914.

See also *Livingstone v. The King*[3]. There are statements in the judgment of this Court in *Wood v. The Queen*[4] which may be difficult to reconcile with the view expressed in the cases cited, but, so far as there is conflict, I think the view expressed in the latter must prevail.

A second general proposition which appears to me to apply in the present situation is stated in *The Queen v. Woodburn*[5], where Sedgwick J., in delivering the judgment of the Supreme Court, said at p. 123:

> It is perfectly clear that a contractor dealing with the Government is chargeable with notice of all statutory limitations placed upon the power of public officers. Where a statute expressly defines the power it is notice to all the world.

Turning now to ss. 41 and 42 of the *Financial Administration Act,* it will be observed that s. 41 prohibits the borrowing of money on behalf of the Crown except with the

[1] June 4, 1959. (Unreported)
[2] (1919) 18 Ex. C.R. 410.
[3] (1919) 19 Ex. C.R. 321.
[4] 7 S.C.R. 645.
[5] (1898) 29 S.C.R. 112.

authority of Parliament and that s. 42 then prescribes what the Governor in Council may do when authority to borrow exists. It is, I think, manifest that the intention of Parliament in enacting these sections is to ensure that money is borrowed only when Parliament has authorized it and that contracts relating to the borrowing of money are made only with relation to borrowing which Parliament has authorized. And since it would be idle for Parliament to enact that in certain situations the Governor in Council might authorize the Minister to enter into contracts relating to the sale of securities if a broader general power to confer such authority were held to exist independently of the statute, in my opinion, s. 42 should be regarded as a definition of the powers of the Governor in Council on this subject. Accordingly, whatever may have been the position prior to the enactment of s. 42(*b*) in 1951, it seems clear that, following its enactment, neither the Minister nor anyone acting on his instructions could have authority to make on behalf of the Crown "a contract relating to the borrowing of the money or the issue or sale of securities relating thereto" unless there was (a) parliamentary authority to borrow the money and (b) an order in council authorizing the Minister to enter into such a contract.

Now parliamentary or statutory authority to borrow money to the extent necessary to pay maturing or redeemed securities which had been issued under the authority of Parliament existed under s. 43 of the *Financial Administration Act* at all times material to these proceedings. But neither in December, 1956 or January, 1957, when the suppliant was first requested to render services in preparation for a twelfth series Canada Savings Bond sales campaign, nor at any time subsequently up to July 10, 1957, when its services were dispensed with, had any order in council been passed authorizing the Minister to borrow by the issue and sale of securities the money necessary to pay maturing or redeemed securities or any other money the borrowing of which had in the meantime been authorized by Parliament, or to enter into contracts relating thereto. In my opinion, the contract in question was one of the kind with which s. 42(*b*) deals, for its object was the sale of securities in connection with the borrowing of money, and it follows, in my

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view, that in the absence of an order in council authorizing the Minister to enter into it, the alleged contract was not binding on the Crown.

Nor, in my opinion, is the position affected by the fact that an order in council was passed on August 20, 1957, authorizing with parliamentary authority the borrowing of money by the sale of Canada Savings Bonds, twelfth series, and the payment out of the Consolidated Revenue Fund of "such expenses as are incurred in connection with the issue and sale" of such bonds. By the time this order in council was passed, the suppliant's services had already been terminated, and I do not think it can be regarded as a ratification by the Governor in Council of any commitment made prior to that time.

It was also submitted on behalf of the suppliant that the Bank of Canada is the statutory fiscal agent of the Government of Canada under the provisions of the *Bank of Canada Act* and that the *Financial Administration Act* has no application to a contract of the kind here in question, but even if these submissions are well founded there is, in my opinion, nothing in s. 20 of the *Bank of Canada Act* or any other section thereof which confers authority on the Bank of Canada to enter into such a contract on behalf of the Crown, and without the authorization of the Governor in Council either to it or to the Minister I do not think the Bank had any such authority.

Nor, in my opinion, is there in the facts existing up to the time of the making of the order in council any basis for a claim against the Crown in quasi contract for the value of the services rendered by the suppliant pursuant to the arrangement. It was suggested in argument that the rule followed in this country differs on this point from that followed in England, but I do not think any case has gone so far as to hold the Crown responsible in quasi contract where the alleged obligation was incurred by a person having no authority to bind the Crown. In *The Quebec Skating Club v. The Queen*[1] Burbidge J., referring to this question, said at p. 400:

> I had occasion in *Hall v. The Queen*, 3 Ex. C.R. 373, to follow the opinion of the learned Chief Justice, though it was expressed with some reserve and in a case which was decided on other grounds. In doing so, however, I thought it proper to add that there might be cases in which some question would arise as to the authority of the officer at whose

[1] (1893) 3 Ex. C.R. 387.

instance the service was rendered. If the Minister of a department, or the officer acting under him, has no authority to bind the Crown in respect of such work or materials, I do not see how a petition of right can lie for the value thereof, and that view is not, it seems to me, opposed to, but, on the contrary, supported by the case of *The Queen v. The Saint John Water Commissioners,* 19 S.C.R. 130, upon which the suppliants rely.

After discussing the *Saint John Water Commissioners* case, Burbidge J. continued at p. 402:

In the case of *Hall v. The Queen,* 3 Ex. C.R. 373, the claimant, to enable certain improvements connected with the Trent Valley Canal to be proceeded with, closed down his mill at the request of the Chief Engineer of Canals, and the officers under him. There was evidence that what was done in reference thereto was, in that case, expressly ratified by the Minister of Railways and Canals, who had power to take possession of the mill and to agree with the claimant as to the amount of compensation, 31 Vict., c. 12, s. 24; R.S.C., c. 39, s. 3, and 52 Vict., c. 13, ss. 3 and 15, and I thought that under the circumstances a promise should be implied on the part of the Crown to indemnify the claimant for the actual loss he had thereby incurred. The Minister might himself have made such a contract, and I could see no good reason why it might not be implied from what his officer with his approval did.

Accordingly, in the view I have of the matter, the suppliant had no right of any kind to relief against the Crown in respect of any services which it had rendered or expenses which it had incurred, either when the services were rendered or the expenses were incurred or in July, 1957, when its services were dispensed with, or at the time when the order in council was passed. There were, however, certain events which occurred afterwards which, in my opinion, afford a basis for relief to a limited extent.

The order in council, which was made on the recommendation of the Minister of Finance, recites that it is desirable to *continue* to provide facilities for the investment of savings by the general public in Government securities, to be entitled Canada Savings Bonds, Series Twelve, and after authorizing the sale of such securities and dealing with their terms and certain matters pertaining to their sale it goes on to give authority to pay out of unappropriated moneys in the Consolidated Revenue Fund "such expenses as are incurred in connection with the issue and sale of Canada Savings Bonds Series Twelve." Statutory authorization to pay such expenses out of the Consolidated Revenue Fund on the authority of the Governor in Council existed in s. 51 of the *Financial Administration Act.* This authorization to pay such expenses out of the Consolidated Revenue Fund is not in itself an express authority to the Minister

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under s. 42(*b*) to enter into contracts relating to the borrowing of the money or the sale of the securities, but reading the order in council as a whole, including its implied reference to earlier Canada Savings Bonds campaigns, in the light of what is shown to have transpired in them, I think it should be interpreted as impliedly authorizing the Minister to incur expenses for advertising and promoting the sale of the bonds as had been done in earlier years. Nor do I think the authority so given or the exercise of it was subject to any further approval by the Treasury Board under the Government Contracts Regulations established pursuant to s. 39 of the *Financial Administration Act*. Section 42(*b*) deals specially with authority to enter into contracts of the kind therein referred to and reserves the granting of authority to enter into them, as well as the terms and conditions of such contracts for the approval of the Governor in Council. Contracts of this kind, in my opinion, are accordingly excepted from the scope of s. 39 and of the regulations established thereunder. From the time of the passing of the order in council, therefore, the Minister in my opinion had authority to arrange for advertising on behalf of the Crown, and the arrangements between the Minister and the Bank of Canada, authorizing the Bank of Canada to make commitments on his behalf, could have effect.

Accordingly, so far as the results of the services rendered by the suppliant were subsequently adopted and used in the campaign, there is, in my opinion, no reason to think that the Crown was not bound to pay for them. The results of the suppliant's services were available, the Crown could repudiate them or adopt and use them if it saw fit, but, in my opinion, if it did adopt or use them an obligation to pay for them would arise, and at that stage the Minister and, through him, the Bank as well had authority to act on behalf of the Crown. In so far, therefore, as use was made in the campaign of the advertising materials which the suppliant had produced or developed or assisted in developing, and in so far as arrangements had been made for broadcasting time and the services of personnel which were subsequently adopted or ratified, I think the suppliant is entitled to recover. *Vide Hall v. The Queen*[1], *The Gresham Blank*

[1] (1893) 3 Ex. C.R. 373.

Book Co. v. The King[1], *The Queen v. Henderson*[2], *The Queen v. Woodburn* (*supra*), *May v. The King*[3]. Nor do I think that s. 30(1) of the *Financial Administration Act* provides a defence to such a claim. That section provides that no contract providing for the payment of any money by Her Majesty shall be entered into or have any force or effect unless the Comptroller certifies that there is a sufficient unencumbered balance available out of an appropriation or out of an item included in estimates before the House of Commons to discharge any commitments under such contract that would, under the provisions thereof, come in course of payment during the fiscal year in which the contract was entered into, and it has been established that no such certificate was issued. This subsection, however, applies only in respect of contracts and, in my view, affords no answer to a claim which is not founded upon a contract. Nor, in my opinion, is the right of the suppliant to recover for its services to the extent that they have been used by the Crown necessarily founded only on contract or the implication of a contract. In *Craven Ellis v. Connors Ltd.*[4], where a plaintiff claiming remuneration for services rendered pursuant to a contract which was held to be void recovered, nevertheless, on a *quantum meruit*, Greer L.J. said at p. 412:

> In my judgment, the obligation to pay reasonable remuneration for the work done when there is no binding contract between the parties is imposed by a rule of law and not by an inference of fact arising from the acceptance of services or goods.

In *Fibrosa Spolka Akcyjna v. Fairbairn Lawson Combe Barbour Ld.*[5] Lord Wright said at p. 61:

> It is clear that any civilized system of law is bound to provide remedies for cases of what has been called unjust enrichment or unjust benefit, that is to prevent a man from retaining the money of or some benefit derived from another which it is against conscience that he should keep. Such remedies in English law are generically different from remedies in contract or in tort, and are now recognized to fall within a third category of the common law which has been called quasi-contract or restitution.

and at p. 63:

> The gist of the action is a debt or obligation implied, or, more accurately, imposed, by law in much the same way as the law enforces as a debt the obligation to pay a statutory or customary impost. This is important because some confusion seems to have arisen though perhaps only in recent times when the true nature of the forms of action have

[1] (1912) 14 Ex. C.R. 236.
[2] 28 S.C.R. 425.
[3] (1913) 14 S.C.R. 341.
[4] [1936] 2 K.B. 403.
[5] [1943] A.C. 32.

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become obscured by want of user. If I may borrow from another context the elegant phrase of Viscount Simon L.C. in *United Australia, Ld. v. Barclays Bank, Ld.*, [1941] A.C. 1, 21, there has sometimes been, as it seems to me, "a misreading of technical rules, now happily swept away." The writ of indebitatus assumpsit involved at least two averments, the debt or obligation and the assumpsit. The former was the basis of the claim and was the real cause of action. The latter was merely fictitious and could not be traversed, but was necessary to enable the convenient and liberal form of action to be used in such cases. This fictitious assumpsit or promise was wiped out by the Common Law Procedure Act, 1852.

The view expressed in the cases referred to has not met with universal acceptance; *vide* Cheshire and Fifoot on the *Law of Contract*, 5th Ed., p. 553 *et seq.*, but it appears to have been the view of Audette J. in this Court in *May v. The King* (*supra*). Audette J. said at p. 347:

> The fallacy of this argument lies *in limine*. Had there been a contract in existence, as alleged, under which the goods had been shipped, the situation would very likely be as he contends. But it must be found that in the present case that at no time there existed a valid contract, and that moreover the right of the suppliants to recover for the goods in classes 1, 2 and 4, under the authority of the *Gresham* case and the several well known cases cited in support of it, such as *Wood v. The Queen*, 7 S.C.R. 645; *The Queen v. Henderson*, 28 S.C.R. 425; *The Queen v. Woodburn*, 29 S.C.R. 112; and *Hall v. The Queen*, 3 Ex. C.R. 373, is a right to recover based, not on an executed contract, because there is no contract extant, but as upon a *quantum meruit*, under the circumstances there stated, where the Crown received the goods among its stock and received full benefit thereof.

I do not think, therefore, that s. 30(1) of the *Financial Administration Act* bars the suppliant's claim on a *quantum meruit*.

It remains to consider the extent to which the suppliant's services were adopted and used and to assess the amount to which the suppliant is entitled therefor. There is uncontradicted evidence that the newspaper advertising, as well as what was called the certificate of intent used in the campaign, bore a similarity of ideas to what the suppliant had developed. There was also such similarity in the newspaper advertising used to advertise television performances. In addition, a clock commercial which had been suggested by the Bank and later developed to some extent by or through the efforts of the suppliant was used. In this case, the suppliant had contracted for work by a film producer who, for the most part, was later paid by McKim Advertising Agency. But the suppliant paid $100 for what had been done at its request.

Use was also made of English television network time which had been reserved by the suppliant, and the form in which the programs were introduced was that which the suppliant had worked on, though it was suggested that two of the four programs were shortened from 90 to 60-minute performances, which presumably would involve a smaller payment for network time. Even so, the evidence indicates that the cost of network time reserved by the suppliant and used in the campaign would be in the vicinity of $60,000. In addition, a budget which had been prepared and submitted by the suppliant at the request of the Bank appears to have been used and, with minor alterations, adopted as the budget for such advertising for the campaign. On the whole of the evidence, I find it impossible to make anything but a very rough estimate of the value of the services which the suppliant rendered and which were made use of in the campaign, but estimating it as nearly as I can, I have come to the conclusion that the value should be set at $13,000.

Accordingly, there will be judgment declaring the suppliant entitled to $13,000, being part of the relief claimed in its petition of right, and costs.

Judgment accordingly.

ONTARIO ADMIRALTY DISTRICT

1962
Jan. 29

BETWEEN:

CANADIAN BRINE LIMITED .....PLAINTIFF;

AND

NATIONAL SAND AND MATERIAL COMPANY LIMITED, WILSON TRANSIT COMPANY and HANNA COAL AND ORE CORPORATION } DEFENDANTS.

Shipping—Practice—Rule 29, General Rules and Orders in Admiralty—Motion to strike out defendants—Motion dismissed.

Held: That where the plaintiff is not certain which defendant or combination of defendants caused the damage complained of which arose out of the same matter all defendants may be joined in the same action as provided in Rule 29 of the General Rules and Orders of the Exchequer Court in Admiralty.

53474-3—11½a

1962

CANADIAN BRINE LTD. v. NATIONAL SAND & MATERIAL CO. LTD. et al.

MOTION to strike out certain defendants.

The motion was heard before Alfred S. Marriott, Q.C., Surrogate Judge in Admiralty for the Ontario Admiralty District at Toronto.

R. F. Chaloner for the motion.

A. J. Stone contra.

MARRIOTT S.J.A. now (January 29, 1962) delivered the following judgment:

This is an application by the defendant National Sand & Material Company Limited for an order that the other defendants Wilson Transit Company and Hanna Coal & Ore Corporation, both of whom carry on business out of the jurisdiction, be struck from the writ as parties improperly joined therein.

The plaintiff's claim as endorsed on the writ of summons is as follows:

> The plaintiff's claim is for damages in the amount of $203,295.53 caused on or about the 25th or 26th day of November, 1958, by the ship *Charles Dick* owned by the Defendant National Sand & Material Company Limited, or the ship S/S *Thomas Wilson* owned at that time by the Defendant Wilson Transit Company, or the steamer *Edward J. Berwind* owned at that date by the Defendant Hanna Coal & Ore Corporation, or any combination of the said ships, in that the ship or ships did collide and interfere with a pipe line and appurtenance situate under the Detroit River between the City of Windsor, in the County of Essex, and the City of Detroit, state of Michigan, United States of America, due to the negligent navigation and operation of the aforementioned ship or ships . . .

It is contended on behalf of the applicant that the other two defendants are not necessary or proper parties to an action against the defendant applicant in the sense that the claims are for separate torts, and the case of *Sadler v. Great Western Railway Co., et al.*[1], is relied on. This is a land case, but in any event it is distinguishable from the present on the facts. In that case the plaintiff had a distinct and separate cause of action against each defendant. Here from the endorsement it appears that the plaintiff is not certain which defendant, or if a combination of two or three caused the damage.

The relevant rule is Rule 29 which provides:

> 29. Any number of persons having interests of the same nature arising out of the same matter may be joined in the same action whether as plaintiffs or as defendants.

[1] [1896] A.C. 450 at 454.

From the nature of the claim as disclosed by the endorsement of the writ of summons; the allegation against each defendant relating to the same dates, it is fair to conclude, keeping in mind the wide language of the Rule, that the three defendants have interests of the same nature, that is an interest to defend themselves from liability for the damage suffered by the plaintiff, which arose out of the same matter. That it is proper to interpret the Rule as being wide in its scope is in accord with the observations of Martin, L.J.A. in *Evans Coleman & Evans Ltd. v. The Roman Prince*[1], where at p. 135, he remarked on the absolute nature of the powers given by Admiralty Rules 29-32 over the interest of parties, and the sweeping language employed by the said Rules. This view is confirmed by the remarks of Lord Phillimore in *Marlborough Hill v. Cowan & Sons*[2], where after pointing out the wide scope of Rule 29 of the Australian Admiralty Court, which was exactly the same as ours, he said at p. 457: "Admiralty jurisdiction originates in the Civil law and never lost touch or connection with it. This procedure was maleable and adaptable." That was a case where the Court approved the joinder of several plaintiffs in an action against a ship.

Other authorities although relating specifically to costs do incidentally establish the rule that where the plaintiff is not certain against whom he has a cause of action, the proper course is to join all defendants in one writ, and the plaintiff will not be allowed the extra costs incurred by bringing separate actions against them. The test generally is whether the plaintiff has acted reasonably; *The Svein Jarl*[3]; *The W. H. Randall*[4]; see also 1 Halsbury 3rd ed. p. 98.

It appears from the nature of the plaintiff's claims as endorsed on the writ of summons that *prima facie* it has acted in accordance with the above principles, and therefore having found that Rule 29 is wide enough to permit joinder of the three defendants in this action, the application must be dismissed at this time, but the order should be without prejudice to a further application being made when the issues are more fully developed, if the defendant is so advised. Costs to the plaintiff in the cause.

Judgment accordingly.

[1] [1924] Ex. C.R. 133.
[2] [1921] A.C. 444.
[3] (1923) 16 Asp. 159.
[4] (1928) P. 41.

1959
Dec. 2
1960
July 7

BETWEEN:

IWAI & CO. LTD. and THE GOSHO COMPANY LTD. ..... } PLAINTIFFS;

AND

THE SHIP *PANAGHIA*, COMPANIA DE NAVEGACION SAPPHO S.A. and ANGLO CANADIAN SHIPPING COMPANY LIMITED ..... } DEFENDANTS.

Shipping—Damage to cargo—Writ of summons—Jurisdiction—Service of writ out of country—Notice—Admiralty Act, R.S.C. 1952, c. 1, ss. 3, 12, 18(3)(4)—Rules 14, 15, 16, 20(d), 21, 24, General Rules of the Exchequer Court in Admiralty—Sufficiency or insufficiency of affidavit of service—Court considers all material before it on motion to set aside order for service ex juris—Bills of Lading Act, R.S.C. 1952, c. 16—Water Carriage of Goods Act, 1936, R.S.C. 1952, c. 291—Appeal from order of District Judge in Admiralty dismissed.

On March 2, 1955, two Japanese corporations commenced an action in the British Columbia Admiralty District as plaintiffs against the Panamanian Steamship *Panaghia*, against Anglo Canadian Shipping Company Limited the charterer of the ship and against Compania Navegacion Sappho S.A., a Panamanian corporation, the owner of the ship, claiming damages to a quantity of pulp carried on the ship from British Columbia ports to Japan. Service of the writ of summons was made in British Columbia on the charterers who entered an appearance and filed a defence. The ship was not arrested but on April 5, 1955, on the plaintiffs' application, leave was granted by Mr. Justice Sidney Smith, D.J.A. to plaintiffs to issue a concurrent writ of summons against the defendant Compania de Navegacion Sappho S.A. and to serve notice of such writ in the Republic of Panama. Such concurrent writ was issued and on May 16, 1955 notice of the writ of summons was delivered to the resident agent of the defendant company in Panama. On the same day the agent sent the notice to New York where, largely by chance (because it was sent to the wrong agents) it reached agents of the defendant company who thought it had been served by mail and upon being advised by British Columbia solicitors that service by post was invalid did nothing about the matter. On March 22, 1957, plaintiffs obtained an interlocutory judgment by default and on July 15, 1957, a copy of the judgment was forwarded to the defendant company's agents in New York. Nearly a year later the plaintiffs proceeded with a reference to assess damages and counsel, instructed by the company's New York agents, appeared on behalf of the company and stated he reserved all defences available to the company. On October 14, 1958, motions were launched on behalf of the company first, for an order setting aside the service and all subsequent proceedings and alternatively setting aside the judgment and giving leave to appear and defend and second, for an order setting aside the writ of summons on the ground that the Court had no jurisdiction to issue it. Smith, D.J.A. ordered that the default judgment be set aside and that the

defendants have leave to defend but upheld the service made on the defendant company and he refused the application to set aside the writ of summons. The defendant company now appeals to this Court from the refusal to set aside the service of the writ and subsequent proceedings.

Held: That the appeal should be dismissed.

2. That Rule 24 of the General Rules and Orders of the Exchequer Court of Canada in Admiralty provides that notice in lieu of service shall be given in the manner in which writs of summons are served and the manner of service of a writ of summons upon a corporation is provided for by Rules 14, 15 and 16 and though the affidavit of service made by the solicitor who delivered the notice falls short of showing that there was valid service under Rule 14, service of Panamanian process upon the resident agent would have been valid service upon the appellant and the Panamanian law came within the words of Rule 15; and further it was not open to the appellant to ignore the service entirely and much later to ask the Court to set it aside.

3. That the responsibility of not knowing the true facts as to the delivery of the notice rested on the appellant, and the Court was justified in refusing to set the service aside merely because of the alleged insufficiency or irregularity in the manner in which it was carried out.

4. That the plaintiffs were justified in bringing action against both defendants as there appeared to be uncertainty as to who were the actual contracting parties.

5. That the action was properly brought against the charterers and the fact that the cargo was loaded in British Columbia and that the provisions of the *Water Carriage of Goods Act, 1936* applied, were sufficient grounds for the Court to entertain the action against the appellant.

APPEAL from an order of the District Judge in Admiralty for the British Columbia Admiralty District.

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

C. C. I. Merritt, Q.C. for appellant (defendant) Compania Navegacion Sappho S.A.

J. R. Cunningham for respondents (plaintiffs).

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

THURLOW J. now (July 7, 1960) delivered the following judgment:

This is an appeal from an order made by Mr. Justice Sidney Smith, District Judge in Admiralty of the British Columbia Admiralty District on an application of the defendant Compania de Navegacion Sappho S.A. to set aside the service of the writ of summons or notice thereof

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and all subsequent proceedings against that defendant and, in the alternative, to set aside a default judgment which had been obtained against that defendant. Smith, D.J.A., set aside the default judgment and gave leave to defend but upheld the service which had been made on that defendant. The defendant now appeals from the refusal to set the service aside.

The action was commenced on March 2, 1955, by the respondents, two Japanese corporations, as plaintiffs against the Panamanian steamship *Panaghia,* Anglo Canadian Shipping Company Limited, a Canadian corporation carrying on business in British Columbia and the charterer at the material time of the ship, and Compania de Navegacion Sappho S.A., a Panamanian corporation, the owner of the ship, as defendants, for damages to a quantity of pulp carried in the ship from British Columbia ports to Japan. The ship was not arrested. On April 1, 1955, the writ of summons was served in British Columbia on the defendant Anglo Canadian Shipping Company Limited, on whose behalf an appearance was entered on April 6, 1955 and a defence was subsequently filed. On April 5, 1955, on the plaintiffs' application, leave was granted by Smith D.J.A. to the plaintiffs to issue a concurrent writ of summons against the defendant Compania de Navegacion Sappho S.A. and to serve notice of said writ in the Republic of Panama. A concurrent writ was, accordingly, issued on April 22, 1955, and on May 16, 1955 notice of the writ of summons was delivered to the resident agent of the defendant Compania de Navegacion Sappho S.A. at Avenida Central 8-40 in Panama City in the Republic of Panama. The delivery of the notice was made by a solicitor who, in his affidavit sworn on the following day and filed on June 16, 1955, gives that address as the office and principal place of business of the defendant in the Republic of Panama.

The resident agent in an affidavit filed in support of the appellant's motion denies that he had any authority under Panamanian law to receive foreign process on behalf of the defendant and states that Avenida Central 8-40 is the address of his law firm, but nowhere in any of the affidavits filed is it denied that that address was the office and place of business of the defendant in the Republic of Panama. At the time of the delivery of the notice, the resident agent declined to accept it, but it was left and later on the same

day he forwarded it to New York, where some ten days afterwards, and largely by chance, because it was in the first instance sent to the wrong party, it reached agents of the defendant Compania de Navegacion Sappho S.A., who apparently had authority to deal with it. These agents appear to have been unaware that the notice had been delivered to the resident agent of the appellant in Panama and to have been under the impression that the plaintiffs' solicitors had attempted to serve the notice by post. They sought advice from British Columbia solicitors as to the validity of the service and, on being advised that service of the notice by post in the United States would not be proper service, they neither caused an appearance to be entered nor, so far as appears, did they make any further inquiries to ascertain the facts as to what had occurred with respect to the notice. Almost two years later, on March 22, 1957, the plaintiffs obtained an interlocutory judgment by default. On July 4, 1957, the plaintiffs' solicitors, as a matter of courtesy, forwarded a copy of the default judgment to the British Columbia solicitors who had been consulted by the appellant and on July 15, 1957, a copy of the judgment was forwarded by the latter to the appellant's agents in New York. Almost a year later, during which evidence was taken on commission in Japan, the plaintiffs proceeded with a reference to assess their damages and, a notice by telegram having been sent to the resident agent of the appellant in Panama of the date fixed for the final hearing on such assessment, counsel, instructed by the appellant's New York agents, attended the hearing on behalf of the appellant and stated that he reserved all defences available to the appellant and that he had no doubt the appellant would wish to apply to set aside the proceedings on the ground that the writ had not been served on it. Thereafter, on October 14, 1958, and October 29, 1958, respectively, motions were launched on behalf of the appellant in the first of which application was made for an order setting aside the service and all subsequent proceedings and, alternatively, setting aside the judgment and giving the appellant leave to appear and defend, and in the second of which application was made for an order setting aside the writ of summons on the ground that the Court had no jurisdiction to issue it. The

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Thurlow J.

grounds argued by the appellant in support of the present appeal and upon which it had asked that the service be set aside were as follows:

(*a*) That Compania De Navegacion Sappho S.A. is not a necessary or proper party to the action and the Order for service ex juris dated the 5th of April, 1955 ought not to have been made.

(*b*) That the affidavit upon which the said Order was made is irregular and insufficient to support the said Order, in that no facts are set out verifying the grounds of the ex parte motion for leave to serve ex juris.

(*c*) That Compania De Navegacion Sappho S.A. was not personally or properly served with the said Notice of Writ of Summons in accordance with the Rules of Court or at all.

With respect to ground (*c*) it is provided by Rule 24 of the General Rules and Orders of the Exchequer Court of Canada in Admiralty that notice in lieu of service shall be given in the manner in which writs of summons are served. The manner of service of a writ of summons upon a corporation is provided for by Rules 14, 15, and 16, which are as follows:

14. A writ of summons against a corporation may be served upon the mayor, or other head officer, or upon the town clerk, clerk, treasurer or secretary of the corporation and a writ of summons against a public company may be served upon the secretary of the company, or may be left at the office of the company.

15. A writ of summons against a corporation or a public company may be served in any other mode provided by law for service of any other writ or legal process upon such corporation or company.

16. If the person to be served is under disability, or if for any cause personal service cannot, or cannot promptly, be effected, or if in any action, whether *in rem* or *in personam*, there is any doubt or difficulty as to the person to be served, or as to the mode of service, the Judge may order upon whom, or in what manner service is to be made, or may order notice to be given in lieu of service.

The affidavit of service made by the solicitor who delivered the notice, in my opinion, falls short of showing that there was valid service under Rule 14 for it does not state that the resident agent of the appellant to whom the notice was delivered was an officer, clerk, treasurer or secretary of the company, nor is the company shown to have been a public company within the meaning of that rule. Nor was the procedure of Rule 16 invoked. It does, however, in my opinion, appear from the several affidavits and the statement of facts filed by the appellant's solicitors that service of Panamanian process upon the resident agent would have been valid service of such process upon the appellant and,

while the statement that the resident agent had no authority under Panamanian law to accept foreign process may well be correct, the Panamanian law, pursuant to which service of Panamanian process might be made on him, appears to me to fall within the meaning of the words "any other mode provided by law for service of any other writ or legal process upon such corporation or company" in Rule 15 when that rule is read in relation to the provision of Rule 24. Moreover, under the English rules corresponding to Rules 14, 15, and 24, it would appear that it is the practice to regard service as good if it is carried out by a method prescribed or authorized by the local law. *Vide Annual Practice 1960,* pp. 116 and 155. In any event, however, and whether or not the delivery of the notice to the resident agent was a mode of service authorized by the Panamanian law in the particular circumstances, I am of the opinion that it was not open to the appellant to ignore entirely the service so made and, at a much later time, to ask the Court to set it aside. A mere enquiry by the appellant's agents of the plaintiffs' solicitors during the 30-day period following the delivery of the notice would have elicited the information that the notice had in fact been delivered to the resident agent in Panama and, if the appellant's agents in New York were at that time lulled into a false security by thinking that the plaintiffs had endeavoured to serve the notice by sending it by post to an address in the United States, the information sent them in July, 1957 that a judgment had been secured should have put them on their enquiry as to how the judgment could have been obtained. Nevertheless, they did nothing until they received through the registered agent in Panama notice of the final hearing upon the assessment of damages. They then made inquiries and learned the facts and subsequently moved to set aside the service and all subsequent proceedings on the grounds which I have set out. In these circumstances, and particularly having regard to the fact that the responsibility for not knowing the true facts as to the delivery of the notice rested on the appellant and to the lack of any adequate explanation as to why the appellant made no move to set aside the judgment or the service in the year following receipt of notice of the judgment, I think the learned Judge was justified in refusing to set the service

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aside merely on the grounds of insufficiency or irregularity, which have been urged, in the manner in which it was carried out.

In the reasons for judgment on the appellant's motion, Sidney Smith D.J.A. did not discuss grounds (*a*) or (*b*), and I do not have the benefit of his reasoning thereon. The explanation for this may conceivably lie in the fact that, strictly speaking, these grounds did not arise on the notice of motion, since they constituted an attack on the order for service *ex juris*, whereas the notice of motion asked only that the service and subsequent proceedings against the appellant be set aside and did not ask that the order for service *ex juris* also be set aside. On the appeal, however, these grounds were argued by both sides without objection on this point by counsel for the respondents, as if the setting aside of the order as well had been asked for, and I think the matter now falls to be determined on that basis.

Of the several instances set out in Rule 20 of the General Rules and Orders of the Exchequer Court of Canada in Admiralty, in which service out of the jurisdiction may be allowed, only that described in clause (*d*) is invoked. This is as follows:

> 20. Service out of the jurisdiction of a writ of summons or notice of a writ of summons, may be allowed by the Judge whenever:—
>
> * * *
>
> (*d*) Any person out of the jurisdiction is a necessary or proper party to an action properly brought against some other person duly served within the district or division in which the action is instituted;

By Rule 21 it is then provided:

> 21. Every application for leave to serve a writ of summons, or notice of a writ of summons, on a defendant out of the jurisdiction shall be supported by affidavit, or other evidence, stating that in the belief of the deponent the plaintiff has a good cause of action, and showing in what place or country such defendant is or probably may be found, and whether such defendant is a British subject or not, and the grounds upon which the application is made; and no such leave shall be granted unless it shall be made sufficiently to appear to the Judge that the case is a proper one for service out of the jurisdiction.

In *The Brabo*[1] Lord Porter, in commenting on the English equivalent of Rule 20(*d*), said at p. 338:

> Primarily the jurisdiction of the courts in this country is territorial in the sense that the contract or tort sued upon must have some connexion with this country or the defendant must be served here. To this principle

[1] [1949] A.C. 326

Or. II, r. I (*g*) is an exception and enables foreigners domiciled abroad to be impleaded in this country provided an action is properly brought against someone duly served within the jurisdiction and the party outside the jurisdiction is a necessary or proper party to that action. The rule is not only an exception to but also an enlargement of the ordinary jurisdiction of the court and should not, in my opinion, be given an unduly extended meaning. The observation of Farwell L.J. in *The Hagen*, [1908] P. 189, 201, and of Lord Sumner in *John Russell & Co. Ld. v. Cayzer, Irvine & Co. Ld.*, [1916] 2 A.C. 298, 304, both quoted by Scott L.J., [1948] P. 33, 39, point out the care which should be taken before the jurisdiction is exercised. No doubt it is in some circumstances desirable that persons not usually subject to the jurisdiction should be brought before our courts in order that a case may be fairly and fully disposed of, but the right to add the foreigner should be sparingly used, more particularly in a case where the party within the jurisdiction may not be subject to any liability and therefore the action would fail as against the only person or persons who could be sued here were it not for the rule.

With respect to the contents of the affidavit required by the English equivalent of Rule 21, in *Chemische Fabrik Sandoz v. Badische Anilin und Soda Fabriks*[1] Lord Davey said at p. 735:

Rule 4 of the same order prescribes that the application is to be supported by evidence stating that in the belief of the deponent the plaintiff has a good cause of action, and no such leave is to be granted unless it be made sufficiently to appear to the court or judge that the case is a proper one for service out of the jurisdiction under this order. This does not, of course, mean that a mere statement by any deponent who is put forward to make the affidavit that he believes that there is a good cause of action is sufficient. On the other hand the court is not, on an application for leave to serve out of the jurisdiction, or on a motion made to discharge an order for such service, called upon to try the action, or express a premature opinion on its merits, and where there are conflicting statements as to material facts, any such opinion must necessarily be based on insufficient materials. But I think that the application should be supported by an affidavit stating facts which, if proved, would be a sufficient foundation for the alleged cause of action, and, as a rule, the affidavit should be by some person acquainted with the facts, or, at any rate, should specify the sources or persons from whom the deponent derives his information.

The affidavit upon which the order for service *ex juris* was obtained in the present case was made by a solicitor, who stated as follows:

1. I am a member of the firm of Macrae, Montgomery, Macrae, Hill & Cunningham, solicitors for the Plaintiffs herein and as such have knowledge of the matters herein deposed to.

2. I am advised by Counsel and verily believe that the Plaintiffs herein have a good cause of action against the Defendant Compania De Naviera Sappho S.A.

[1] (1904) 90 L.T. 733.

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3. In my belief the said Defendant is situated in the City of Panama in the Republic of Panama and is not a British subject.

4. The application herein for leave to issue a Notice of the Writ of Summons herein on the said Defendant Company is made upon the grounds that the said Defendant Company is a proper party to the Action herein properly brought against the Defendant Anglo Canadian Shipping Company Limited.

5. That the said Defendant Anglo Canadian Shipping Company Limited has been duly served within the British Columbia Admiralty District as evidenced by the Affidavit of Service of this deponent sworn the 1st day of April, 1955 and filed herein.

This affidavit, in my opinion, falls far short of disclosing a case for service *ex juris* under Rule 20(*d*). Nowhere in it is there any statement of what cause of action the plaintiffs have against the defendant Anglo in respect of which the action is brought, and the deponent does not even state that he believes the plaintiffs or either of them has a good cause of action against that defendant. And nowhere in the affidavit are any facts stated showing that the plaintiffs have any cause of action against that defendant. Such facts are, in my opinion, essential, for without a cause of action being shown against that defendant there is no foundation for the application of Rule 20(*d*), nor is there anything upon which the Court can determine either that the action is "properly brought" against that defendant or that the foreign defendant is a necessary or proper party to such action. For this purpose, the statements in paragraph 4 of the affidavit are entirely insufficient, being nothing but the deponent's opinion or submission on a matter which it is the function of the Court to determine. Moreover, while the deponent states that he is advised by counsel and verily believes that the plaintiffs have a good cause of action against the foreign defendant, nothing is disclosed as to what that cause of action is or what connection it has with the cause of action, if any, in respect of which the defendant Anglo has been joined. Nor does the affidavit disclose any facts upon which the discretion of the Court to grant leave in the particular case might properly be exercised. Moreover, neither the endorsement on the writ nor the statement of claim which was subsequently filed can take the place of evidence and fill these defects. *Empire-Universal Films v. Rank*[1].

Accordingly, were there nothing more to the case it would follow that the leave granted by the order should not be sustained, but in my opinion there are two reasons in this

[1] [1948] O.R. 235.

case why that result does not follow. First, there is the matter of delay to which I have already referred. The appellant's solicitors knew the contents of this affidavit from the time of the earliest inquiry, and even if the appellant's agents can, in the peculiar circumstances, be excused for not making any move against the order during the two years that followed, insofar as their motion and appeal are based on deficiencies in the affidavit I do not think their inaction in the year after they had notice of the default judgment can be overlooked. In *Reynolds v. Coleman*[1] Cotton L.J. dealt with a similar situation as follows at p. 461:

> This is a motion to discharge an order giving leave to serve notice of a writ out of the jurisdiction. That order was made more than a year before this application; and by virtue of service pursuant to that order, judgment was obtained in June, 1886, on the ground that the Defendant had not delivered a defence. The Defendant who is now moving does not apply on an affidavit of merits asking for leave to defend, but seeks to have the order for service discharged on several grounds.
>
> He has raised objections to the affidavit on which the order was obtained—that there was not sufficient disclosure of the real facts of the case, and that the Court was not properly informed of matters of which it ought to have been informed. Now, I do not for a moment intimate an opinion that persons applying for *ex parte* orders of this kind ought not fully and fairly to state the facts on which their application depends, but fully as I adhere to that rule, it is in my opinion too late for the Defendant, who has lain by without taking any step for more than twelve months, to ask us to interfere on the ground of those alleged irregularities, however much we might have attended to them if, immediately after the service had been made, he had applied on those grounds to discharge the order for service. Supposing, then, that he could have maintained those objections to the contents of the affidavit if he had come earlier than he has, I am of opinion that we cannot attend to them now.

The other reason why it does not follow from the mere insufficiency of the affidavit that the order for service *ex juris* should be set aside is that the question before the Court on an application to discharge an order for service *ex juris* is not merely whether the affidavit used to lead the order was sufficient for that purpose but whether on the whole of the material before the Court, when the motion is made to set the order aside the case is a proper one for service *ex juris* under the rules. *Vide The Brabo* (*supra*) and Annual Practice 1960, p. 154 and cases there cited. In

[1] (1887) 36 Ch. D. 453.

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Chemische Fabrik Sandoz v. Badische Anilin und Soda Fabriks (*supra*) Lord Davey appears to have considered the problem in this way when he said at p. 735:

> In the present case, if I had been in Joyce, J.'s place, I am not sure that I should have granted the leave for service abroad on Mr. Johnson's affidavit alone, but on the affidavits filed by the present appellants I think that there was enough to justify the learned judge in refusing to discharge the order.

In some cases the plaintiff, asking at a late date to file supplementary affidavits, has, in the exercise of judicial discretion, been refused leave to do so—*vide Empire-Universal Films v. Rank (supra)*—but in the present case the order appealed from recites that it is made upon reading an affidavit made by the master of the *Panaghia* and several other affidavits filed by the present appellant, several further affidavits filed by the respondents, statements of the facts pertaining to the proceedings filed by the solicitors both for the appellant and the respondents, and "the pleadings and proceedings in this action." The "proceedings" appear to include the evidence taken on commission in Japan which was sent up as part of the record on this appeal. Together, these add a considerable body of facts beyond the meagre information contained in the affidavit upon which the order was obtained. Whether the affidavits and other material filed on behalf of the respondents were admitted by consent or without objection or in spite of objections thereto does not appear, but I think I must assume that they were received and are properly before the Court. In any case, I see no good reason why they could not properly have been received by the learned judge and taken into account in determining the question before him, and I am of the opinion that they can now be taken into account in reviewing his refusal to revoke the leave to serve *ex juris*. If, therefore, the present appeal is to succeed, it must do so on the ground that on the whole of this material the case is not a proper one for service *ex juris* upon the appellant under the rules.

From the affidavits and other material, it appears that, at the material times, the *Panaghia* was owned by the appellant and was under a voyage charter to the defendant Anglo, that in February, 1954, the *Panaghia* loaded in British Columbia a general cargo, including pulp consigned to the respondents, that the bills of lading for the pulp, upon which

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the respondents sue, showed the pulp received on board the *Panaghia* in apparent good order and condition, and that, upon arrival in Japan, the pulp was found to have suffered damage from a number of causes, among which were moisture from other cargo stowed in the same holds with the pulp and coal dust which remained in the holds after carrying coal cargoes on previous voyages. Accordingly, having regard to the *Bills of Lading Act* and the *Water Carriage of Goods Act, 1936,* the provisions of which latter act were expressly incorporated in the bills of lading for the pulp in question, in my view, it sufficiently appears that the respondents have a plausible cause of action in contract against the carrier. Now, the bills of lading are signed by an individual with the addition "for and by authority of Master" which, though they do not bear the appellant's name, suggests at once that the appellant is the other party to them. On the other hand, they do bear the name of the defendant Anglo, and it was on behalf of Anglo and pursuant to its instructions that the master signed an acknowledgement of damage to the pulp on arrival, and there is, in my opinion, on the whole of the material a substantial question as to who, on the facts, was the carrier and the other party to the bills of lading. In *Carver's Carriage of Goods by Sea,* 10th Ed., it is pointed out at pp. 286 et seq. that the question as to who is responsible to the shippers for the performance of the contract of carriage made with them is one of fact depending on the documents and circumstances of each case and that uncertainty arises when the contract has been made with the master, for he may possibly be regarded as agent either for the owner or the charterer. In the present situation, there being uncertainty as to which of the defendants was the other contracting party, the plaintiffs were, I think, justified in bringing their action against both of them, and I am accordingly of the opinion that the material sufficiently shows that the action is properly "brought" against the defendant Anglo and that the appellant is a proper party to it within the meaning of Rule 20(*d*). *Massey v. Heynes*[1].

A case falling within the strict requirement of the rule having thus been shown, the circumstances that the cargo was loaded in British Columbia and that the provisions of the *Water Carriage of Goods Act, 1936* apply afford, in my opinion, sufficient grounds for the exercise of the Court's

[1] (1888) 21 Q.B.D. 330.

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discretion to entertain the action as against the appellant. The judgments in *Boston Law Book Company v. Canada Law Book Company Ltd.*[1] and *Beaver Lamb and Shearling Co. Ltd. v. Sun Insurance Office, London, England*[2], which were cited on behalf of the appellant, in my opinion are clearly distinguishable on their facts.

On the whole, therefore, I am of the opinion that there was sufficient material before the learned Judge upon which he could conclude that this was a proper case for leave to serve the appellant *ex juris* under Rule 20(*d*) and, in the words of Lord Davey in *Chemische Fabrik Sandoz v. Badische Anilin und Soda Fabriks,* to "justify [him] in refusing to discharge the order."

On the hearing of the appeal, counsel for the appellant also argued that the action could not be regarded as *properly brought* against the defendant Anglo because none of the clauses of s. 20(1) of the *Admiralty Act* was applicable and the plaintiff therefore had no right to commence the action in the British Columbia Admiralty District. In another appeal[3] in this action taken from the refusal of the learned Judge to set aside the writ of summons on the ground that the Court had no jurisdiction to issue it, I have come to the conclusion that s. 20(1) is not an exhaustive statement of the instances in which actions may be commenced in the several registries of the Court and that the Court had jurisdiction to issue the writ in this case since the endorsement on it shows claims of a kind over which the Court has jurisdiction. The defendant Anglo having been resident in British Columbia, where it was in fact served shortly after the writ was issued, I am of the opinion that the action was *properly brought* against it in the British Columbia Admiralty District.

The leave to serve the appellant *ex juris* and the service made pursuant to such leave will accordingly be sustained, and the appeal will be dismissed with costs.

Judgment accordingly.

[1] 43 O.L.R. 13.

[2] [1951] O.R. 401.

[3] [1960] Ex. C.R. 499.

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Apr. 27
Dec. 14

BETWEEN:

THE ROYAL TRUST COMPANY, JOHN WHITE HUGHES BASSETT and CHARLES H. PETERS, Executors of the Last Will and Testament and of a Codicil thereto of the late JOHN BASSETT .. APPELLANTS;

AND

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

Revenue—Dominion Succession Duty Act, R.S.C. 1952, c. 89 and R.S.C. 1952, Supplement, c. 317, s. 3(1)(g)—"Succession"—Pension to widow not provided by deceased husband—Non-contributory annuity provided by employer of deceased husband—Voluntary and benevolent undertaking on part of employer in recognition of past services—Capitalized value of annuity added to succession by Minister—Appeal from assessment allowed—Date of acquiring vested interest in the annuity—Calculation of value of interest—Civil Code, Article 1029—"Accruing or arising by survivorship or otherwise on the death of the deceased".

The abovenamed deceased, John Bassett, who died on February 12, 1958, was at the time of his death and had been for many years prior thereto a director and officer of the Gazette Publishing Co. Ltd. of Montreal, Quebec. On March 27, 1947 the company entered into an agreement which recited that Mr. Bassett had served the company in diverse capacities and offices throughout many years but that he was not entitled to any benefit under any existing pension plan of the company and that the company desired to enter into an agreement not only with regard to his continuing remuneration, so long as he should be president of the company but also appropriately recognizing his long and effective service in the company's interest. It provided for the payment of a pension to him for his lifetime on his ceasing to be the company's president and that after his death it would pay to his wife during her lifetime if she survived him a pension at the rate of $5,000 per year and that the benefits so provided were in recognition of the valuable services rendered by him to the company prior to the execution of the agreement. The capitalized value of the annuity to the widow was added by the Minister of National Revenue to the assets of the succession of the deceased and taxed accordingly. From that assessment the executors of the will of Mr. Bassett appeals to this Court.

Held: That the annuity was not provided by the deceased but was of a non-contributory nature and constituted a benevolent undertaking on the part of the company for the deceased's past services which had been fully paid for and acquitted and could not form the basis for any further claim against the company by the deceased or his widow, and by accepting a guaranteed minimum salary from the company Mr. Bassett could not be said to be sacrificing his own interest in order to benefit his wife.

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2. That the widow acquired a vested right in and to the annuity upon the execution of the agreement of March 27, 1947 providing for it even though contingent on her surviving her husband and it had an appreciable value in 1947 by reason of the difference in age of the husband and wife.

3. That the appeal must be allowed.

APPEAL under the *Dominion Succession Duty Act.*

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

John deM. Marler, Q.C. for appellants.

A. H. Graham Gould, Q.C. and *Paul Boivin, Q.C.* for respondent.

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

KEARNEY J. now (December 14, 1961) delivered the following judgment:

This is an appeal by the above-mentioned executors of the will of the late John Bassett, publisher, in his lifetime of the city of Montreal, from an assessment levied by the respondent under s. 3(1)(*g*) of the *Dominion Succession Duty Act,* R.S.C. 1952, c. 89, and R.S.C. 1952, Supplement, c. 317.

The issues in this appeal arose because the appellants allegedly had omitted to include among the assessable assets of the Succession of the late John Bassett (hereinafter sometimes called "the deceased"), who, up to the time of his death and for many years prior thereto, had been a director and officer of The Gazette Printing Co. Ltd. of Montreal, P.Q., the capitalized value amounting to $54,033.85 of an annuity payable by the said Company to the deceased's widow. The Minister considered that the above-mentioned amount was subject to duty under s. 3(1)(*g*) of the Act as aforesaid, added the said amount to the assets of the Succession and taxed it accordingly. The relevant provisions of the above-mentioned section read thus:

3. (1) A "succession" shall be deemed to include the following dispositions of property and the beneficiary and the deceased shall be deemed to be the "successor" and "predecessor" respectively in relation to such property.

(*g*) any annuity or other interest purchased or provided by the deceased, either by himself alone or in concert or by arrangement with any other person, to the extent of the beneficial interest accruing or arising by survivorship or otherwise on the death of the deceased, . . .

The appellants contested the applicability of s. 3(1)(*g*) and appealed from the said added assessment, but on review the Minister affirmed it.

The parties agreed that the widow was in receipt of an annuity and that it was not purchased by the deceased and that its value, subsequent to his death, amounted to $54,033.85.

As appears more fully by the appellants' amended statement of claim, they deny: (a) that the annuity was provided by the deceased; (b) that any interest accrued or arose on said decease, since, by reason of an agreement, dated March 27, 1947, entered into between the deceased and the Company, and to which the widow was made a party, she in principle but not in value had exactly the same rights in the annuity prior to her husband's death as she had subsequent thereto. Alternatively, even if it is admitted that the annuity was purchased or provided by the deceased and that a beneficial interest accrued or arose upon the death of her husband, any additional assessment must be limited to the difference if any between the value of Mrs. Bassett's rights or interest prior and subsequent to the decease of the husband.

In respect of the amount of such difference, it was submitted that, if the valuation were made an instant before and an instant after her husband's demise or in *articulo mortis* (as it is sometimes described), the value of the widow's interest would not be materially less than $54,033.85, in which case no additional tax could be levied. But if the said valuation were made as of the date on which the deceased attained his 72nd year, his wife's interest, provided of course she were then alive, would amount to $21,547.60 instead of $54,033.85 as claimed and the respondent would only be entitled to add to the assessable value of the deceased's estate the difference between the foregoing amounts, namely $32,486.25.

The material facts disclosed by the record and the oral evidence, which was brief, is neither contradictory nor disputed. The following admissions in writing were filed by the parties:

1. The said late John Bassett died on February 12th., 1958;

2. The said late John Bassett was born on February 7th, 1886, and was therefore 72 years of age at the time of his death;

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3. The said late John Bassett left a Will dated October 4th, 1947, and one Codicil thereto dated April 7th, 1955, both probated in the Superior Court, District of Montreal, on March 5th, 1958;

4. Appellants are the Executors of said Will and Codicil;

5. The wife of the late John Bassett, Marion Wright Avery, was born on May 10th, 1894. At the time of her husband's death, which she survived, she was therefore 63 years of age and she is still living;

6. The value of an annuity of $5,000 per annum, payable in monthly instalments, to a person aged 63 beginning upon the death of a person aged 72 years is the difference between the value of such an annuity on a life aged 63 and the value of such an annuity on the two lives and is the sum of $21,547.60 provided both are alive at time of valuation.

(see Ex. 2).

As appears by Exhibit 4, the vice-president and secretary-treasurer of the Company, being duly authorized for the purpose (Ex. 5), signed on behalf of the Company the previously referred to agreement dated March 27, 1947.

In the preamble of the said agreement it is stated that Mr. Bassett had served the Company in diverse capacities and offices throughout many years, but that he was not entitled to any benefit under any existing pension plan of the Company, and that the Company desired to enter into an agreement, not only with regard to his continuing remuneration, so long as he should be president of the Company, but also with regard to the provisions appropriately recognizing his long and effective service in the Company's interest in the past. The body of the agreement recites, *inter alia*, certain undertakings by the Company, the most relevant of which are substantially as follows:

(*a*) that so long as the deceased continued to be its president, it would pay him at the same rate of salary (exclusive of bonuses) paid to him in respect of the year 1945 and would continue at its expense to place at his disposal the same facilities as were available to him throughout that year and that on the deceased's ceasing to be its president it would pay him during his lifetime a certain pension; and the deceased undertook that when entitled to receive the pension provided for as aforesaid he would not, without the consent of the Company, become an officer, director or employee of or acquire any financial interest in any newspaper not owned or operated by the Company either alone or with others (with the exception, in certain circumstances, of The Sherbrooke Record) and would not devote to the affairs of The Sherbrooke Record any larger portion of his time or energies than the average devoted by him during the three calendar years ending on December 31st, 1941.

(*b*) that the Company undertook that as and from the deceased's death it would pay to his wife during her lifetime, should she survive him, a pension at the rate of $5,000 per annum, payable by even and equal monthly installment of $416.66 each.

(c) that the benefits so provided to be received by the deceased and by his widow should she survive him were in recognition of the valuable services rendered by the deceased to the Company prior to the execution of the Agreement and should in no way be affected or invalidated by any failure or inability from whatsoever cause or reason on the part of the deceased to fulfil any or all of his obligations connected with his office of president of the Company and that the Company was not precluded from paying to the deceased such bonus or bonuses or additional remuneration as the directors of the Company might at any time or times in the future in their discretion decide upon.

The first and main issue depends on the interpretation to be given in the light of the circumstances to the word "provided".

As far as I am aware, Canadian jurisprudence is lacking on the above-mentioned question, but the relevant provisions of s. 3(1)(*g*) were taken from and are identical to s. 2(1)(*d*) of the *Finance Act* of 1894 which has received judicial consideration in England.

In *Bibby & Sons, Ltd. v. Inland Revenue Commissioners*[1] it was held that s. 2(1)(*d*) was inapplicable because the widow had no established beneficial interest in or enforceable right to the annuity against the Company because the trustees of the pension fund had unfettered discretion as to its disposition. But Harman J., dealing with the question of whether an annuity or pension payable to the widow was *provided* (emphasis supplied) or purchased by the deceased, stated at page 487:

I would add, if it be necessary, that, in my judgment, this annuity, if it be an annuity and if the interest of the plaintiff be a beneficial one, is not an annuity provided or purchased by the deceased. Certainly it is not purchased, because he did nothing to purchase it. He made no bargain, and he did not come into the company's employment under the promise, express or implied, of a pension. He had, as I say, satisfied all the conditions of the pension deed before the deed was ever in existence, and there is no evidence that he ever changed his position thereafter or stayed longer or did more work or got less pay because of the existence of the deed. It is said, however, that he provided the pension because he was, as I say, the sine qua non of its payment. That does not seem to me to be enough. It seems to me that the person who provided it was the company. They put up all the money and through their agents, the trustees, might or might not distribute it to certain persons who were the objects of the company's bounty. Therefore, I hold also that the deceased did not provide the pension.

[1] [1952] All E.R. 483.

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Commenting on the interpretation to be given to the word "provided", the following remarks are found in Green's *Death Duties*, 4th ed., p. 155:

> If the deceased did not contribute directly, the benefit cannot be said to have been provided by him merely by reason of his services to his employer. Duty will be payable under a non-contributory scheme only if the deceased provided the benefit in some other way, e.g., by surrendering part of his own pension; or where the provisions of s. 30(1) of the Finance Act, 1939, apply.

Likewise, in the tenth edition of Hanson's *Death Duties*, under the title of *Pension and Provident Funds*, p. 272, No. 629, it is said:

> No duty is payable under the subsection where the deceased made no pecuniary contribution to the fund out of which the benefit is paid unless the benefit arising was secured by the deceased giving up part of his own benefit under the scheme. If the deceased made some contribution and the employers also contributed, duty may be payable on the whole benefit arising on the ground that it was provided by the deceased in concert or by arrangement.

I think the reasoning in the above-mentioned authorities is applicable in the present case. Exhibits 4 and 5 and the testimony of Charles H. Peters, president of The Gazette Printing Company and formerly its vice-president, is proof, in my opinion, that the late John Bassett did not deplete his patrimony in order to benefit his wife. He had no legal right to any annuity prior to 1947. The annuity which his wife became entitled to thereafter was of a non-contributory nature and constituted a benevolent undertaking on the part of the Company. What motivated the Company in granting the annuity was the deceased's past services, which had been fully paid for and acquitted and could not form the basis for any further claim against the Company by him or his widow.

It was stressed on behalf of respondent that the deceased, in agreeing to accept for the future, so long as he held the office as president of the Company, the same salary as was paid him in respect of the calendar year 1945, in a measure provided his wife's annuity [Ex. 4, para. (1)].

Paragraph (1) of the agreement must be read in conjunction with paragraph 8, which provides that nothing in paragraph (1) will preclude the Company from paying Mr. Bassett any bonuses or additional remuneration, as the directors may at any time see fit to pay after taking into consideration the services rendered by the deceased and the then financial position of the Company.

In 1956, when Mr. Bassett ceased to be president and became chairman of the Board, his duties declined considerably, but Exhibit 6 shows that, beginning in 1955 until he died in 1958, the deceased's annual remuneration, including bonuses, was about $3,000 in excess of what he received in 1947 when the agreement was signed.

Under other circumstances, it might be said that by accepting to work for the Company at the same rate of salary he sacrified his own interest to benefit to his wife, but I do not think that such a conclusion is warranted in the instant case. On the contrary, I think it is true to say that by accepting a guaranteed minimum salary the late Mr. Bassett, far from sacrificing his own interest in order to benefit his wife, did himself a signal service. Mr. Peters' evidence discloses that, although the deceased "died in harness", he was confined to an invalid's chair due to a tubercular hip during the last fifteen years of his life, was an excellent salesman but his activities in this respect were greatly restricted by this incapacity, his general health was poor and his hip trouble was increasing. For the Company, under the circumstances, to guarantee the deceased a non-diminishing salary, which was binding on it, notwithstanding a possible sale by the owners of their controlling stock interest in the Company, in my opinion, without detracting from the deceased's loyalty and devotion to the Company's interests, constitutes additional evidence of the Company's attitude of benevolence. Although the deceased had never asked for an increase in salary or a pension, the directors of the Company were aware that when his incapacity became permanent at the age of 61, he was greatly worried about the future, particularly as his stock interest in the Company was negligible and he had to provide for a wife who was nine years his junior. According to Mr. Peters, without consulting Mr. Bassett the directors of the Company decided to establish, in favour of himself and his wife, separate annuity benefits fashioned on the form in general use in the banking world, and when the decision was made known to the late Mr. Bassett, he and his wife accepted it with gratitude and enthusiasm.

Counsel for the respondent submitted as a further argument that we were here dealing with a stipulation *pour autrui* by a husband in favour of his wife, as envisaged by article 1029 C.C. I do not think this to be the case because

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the word "stipulate" implies authority and connotes the action of specifying or laying down certain conditions. In my opinion the facts disclose that the deceased was in no position to stipulate for himself, much less for his wife, and it was the Company which was in complete control of the situation and which determined the conditions of the annuity. Insofar as both beneficiaries were concerned, it only remained for them to accept or refuse the Company's offer. For the foregoing reasons I conclude that the respondent has failed to establish that the annuity in issue was provided by the deceased.

Did the beneficial interest accrue or arise on the death of the deceased?

In seeking to determine whether such an interest accrued or arose within the meaning of s. 2(1)(*d*) of the *Finance Act* (*supra*), Lord Morton of Henryton in *D'Avigdor-Goldsmid* and *Inland Revenue Commissioners*[1] made the following observations (p. 366):

> There are three conditions which must be satisfied in order to give rise to a claim for duty under section 2(1)(*d*), namely:—
>
> (i) There must be an annuity "or other interest"; (ii) It must have been "purchased or provided by the deceased, either by himself alone or in concert or by arrangement with any other person"; and (iii) A beneficial interest therein must accrue or arise by survivorship or otherwise on the death of the deceased.

In respect of condition (iii) it was submitted by the respondent, on whom the burden lies, that Mrs. Bassett "had no right (beneficial interest) whatever until the death took place" and, on the death, the beneficial interest accrued or arose; and alternatively, that any right she might have possessed prior thereto "had no value at all" and consequently her beneficial interest could only arise subsequently to her husband's death.

It is difficult for me to see how the respondent, having admitted that, according to accepted actuarial tables, the expectant interest of the widow, calculated when the deceased was alive and on the day he attained his 72nd birthday, was $21,547.60, can now be heard to say that she had no beneficial right during the lifetime of her husband and that, if she had, it was worthless.

[1] [1953] A.C. 347.

In my opinion, upon the execution of Exhibit 4 Mrs. Bassett acquired a vested right in and to the $5,000 annuity. True it was contingent, in the sense that it was only enforceable provided she and her husband were not divorced and she survived him, but it was binding on the Company, and notwithstanding that its value was subject to heavy discount during the lifetime of the deceased; nevertheless, it had an appreciable value in 1947 by reason of the difference in age of the two parties concerned.

The difficulty involved in properly interpreting the meaning of the words "accrue" and "arise", as used in condition (iii), may be gathered from the conflicting views expressed thereon in the relatively recent case of *Westminster Bank v. Inland Revenue Commissioners*[1].

Briefly, the case, which in some respects is apposite, concerned two settlements, one made in 1929 and the other in 1932. I shall refer only to the second one, wherein a settlor assigned to a trustee four fully-paid policies on his life, directing him to hold the same in trust for his four sons, and, on the settlor's death, to divide the proceeds of the policies in certain proportions among them—one of whom was given a life interest.

It was held (reversing the Court of Appeal, Lord Reid and Lord Radcliffe dissenting) that estate duty was not payable under s. 2(1)(*d*) *supra* because the beneficial interest of the four sons in the proceeds of the policies did not accrue or arise on the death of their father.

Lord Keith at page 236 summarized the respondents' argument as follows:

> . . . . if the life-tenant could not demand of the trustees that the policy should be converted into an interest-bearing asset during the lifetime of the settlor, there was in the life-tenant only an interest in expectancy, which became an interest in possession of the life-tenant on surviving the settlor. This, it was said, was a beneficial interest in the policy provided, accruing or arising by survivorship on the death of the settlor.

Then, after quoting the *D'Avigdor-Goldsmid* case, wherein the interest provided was an absolute and an indefeasible one on the death of the settlor and wherein it had been decided that no beneficial interest arose on the death of the settlor, His Lordship went on to say at page 237:

> I would examine the argument, however, more fully. It is obvious, in the circumstances postulated, that if the life-tenant fails to survive the settlor, he will get no enjoyment of what has been provided for him.

[1] [1958] A.C. 210.

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That of itself seems to me to be a circumstance of little importance. It might be said to be merely a matter of degree. If he survives the settlor he may live to enjoy his life-interest only for a day, or a week, or a month. A person absolutely entitled may also not survive to enjoy the benefit provided. The benefit, it is true, in the fulness of time will fall into his estate, or he may sell it during his life and before the settlor's death, suitably discounted. But these are differences due to the nature of the interest provided. The one must bear full fruit; the other may wither in the bud. If the life-tenant survives to enjoy what has been provided he takes, not by virtue of a beneficial interest accruing or arising by survivorship, but because the interest provided has begun to bear fruit.

And at page 237:

It would be a remarkable thing, in my opinion, that where the right at the death is cut down to a life interest (as in the instant case) a different result should follow.

Lord Keith of Avondale stated at p. 235:

I would observe also that it is the interest provided that is to be deemed to pass at the death, but the value of this interest is quantified, for the purposes of duty, by the extent of the beneficial interest accruing or arising by survivorship at the death.

Because I have already come to the conclusion that the respondent has failed to satisfy condition (ii), I think it is unnecessary for me to determine whether or not condition (iii) has been fulfilled.

I will pass on to the question of whether—a), assuming that the deceased provided the annuity and it accrued or arose upon his death, the additional assessment in question should be limited to the excess value of the widow's right or interest after the death of her husband over its previous value prior thereto; and b), if so, in what manner should such difference be determined.

I think query a) should be answered in the affirmative.

Of course, no two cases are the same, but in *Adamson v. Attorney-General*[1], wherein it was established that a child's interest had been provided by the deceased, Lord Warrington of Clyffe stated at page 277:

. . . . In the present case the interest of each child was unquestionably provided by the deceased, and is therefore to be deemed to be included in the expression "properly passing on the death of the deceased," but only to the extent of the beneficial interest accruing or arising on the death of the deceased.

Following the *Adamson* case a retroactive amendment was made to the *Finance Act* of 1934, whereby it was provided that for the purposes of s. 2(1)(*d*) of the *Finance Act, 1894,*

[1] [1933] A.C. 257.

the extent of any beneficial interest accruing or arising by survivorship or otherwise on a death shall be ascertained without regard to any interest in expectancy that the beneficiary may have had before the death. This amendment was designed to nullify the effect of the decision in *Adamson v. Attorney-General* referred to above. However, no corresponding amendment to the *Dominion Succession Duty Act* has been made and I believe that the principle laid down in the *Adamson* case is still applicable to cases arising under the *Dominion Succession Duty Act*.

In a later case, *Attorney-General v. Lloyd's Bank Ltd.*[1], which was a matter in which the issue turns on a settlement and a deed of appointment in which the settlor reserved a power of revocation by deed or will but died without having revoked the appointment, it was held that the life interest of each child (which was absolute and immediate though liable to defeasance) was within s. 2(1)(*d*) of the *Finance Act, 1894,* but that the duty thereunder was leviable only on the excess, if any, of the value of the expectant life interest of each child after the death of the settlor over its previous value.

b) How should any excess be determined?

As appears by an amended statement of claim filed with the permission of the Court, the appellants averred that the comparable value of the widow's interest in expectancy, if determined an instant before and an instant after the deceased's death, would have been for practical purposes the same and no Succession Duty tax would be exigible.

In support of this latter submission reliance was placed on (i) the *D'Avigdor-Goldsmid* case and particularly on the observations therein of Lord Porter, where he stated at page 365:

> My Lords, the difference between the moment when an assured man is in articulo mortis and the moment of his actual decease must be infinitesimal and I am not convinced, as at present advised, that the law would pay attention to so minute a sum.

and (ii) the evidence on cross-examination of the respondent's actuary Walter Riese, wherein he conceded that the value of the annuity at the two instants above-described "would certainly be very close".

[1] [1935] A.C. 382.

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The appellants concede that on the death of the deceased the value of his widow's annuity was properly arrived at in accordance with s. 35 of the Act which reads as follows:

> 35. The value of every annuity, term of years, life estate, income, or other estate, and of every *interest in expectancy* in respect of the succession to which duty is payable under this Act shall for the purposes of this Act be determined by such rule, method and standard of mortality and of value, and at such rate of interest as from time to time the Minister may decide (emphasis supplied).

In order to place the value of $54,033.85 on the widow's annuity following the death of her husband, the respondent made use of the actuarial method of determination.

As we have seen, the widow's interest in expectancy, calculated as of the 72nd birthday of the deceased, when both he and his wife were alive, amounts to $21,547.60, but counsel for the appellants submits by his amended statement of claim that the comparable value of the widow's interest in expectancy, if determined an instant before and an instant after the deceased's death, would have been for practical purposes the same and no tax was exigible.

Bearing in mind that the subject-matter to be evaluated is an interest in expectancy, I believe that the-instant-before-and-after method is self-defeating because it only becomes applicable when the event the uncertainty of which gives rise to the expectancy has taken place. Even were the above method highly commendable, the Minister, who under s. 35 of the Act is endowed with broad discretionary power, has not seen fit to adopt it for succession duty purposes; consequently, I think its applicability to the instant case can be disregarded.

The difference between the two methods becomes apparent if one considers that, when the deceased attained his 72nd birthday, actuarially speaking his expectant life span had several years to run, but, as shown by subsequent events, it was in fact limited to less than a week.

If, assuming that s. 3(1)(*g*) were applicable and it became necessary for me to determine the extent of the widow's interest accruing or arising on the death of the deceased, as presently advised, and in the absence of any evidence of a contrary valuation, I would be disposed, for the foregoing reasons, to hold that it would be the difference

between the $21,547.60 previously mentioned and the amount of $54,033.85 claimed by the respondent, namely the sum of $32,486.25.

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Kearney J.

Since, for reasons given earlier, I consider that the respondent has failed to establish that the present case falls within the purview of s. 3(1)(*g*), I maintain the appeal with costs.

Judgment accordingly.

BETWEEN:

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

1962

Jan. 18

Feb. 22

AND

CHARLES AUGUSTE BEGIN .....RESPONDENT.

Revenue—Income tax—Partnership formed to sell beer—Profits used wholly for community welfare—Whether tax exempt as a charitable or non-profit organization—Income Tax Act, R.S.C. 1952, c. 148, ss. 6(c), 15(1), 62(1)(e) and 62(1)(i).

At a meeting of the leading citizens of the town of Mont-Joli it was decided that application be made to the Quebec Liquor Commission for the issue of a single licence for the sale of beer in the town and that the profit from such sale be used for social welfare, education and civic improvement. At the request of the meeting the respondent and two others agreed to supervise the distribution of the profits and following the issuance of a licence to him, the three entered into a partnership under the name of "Distributors Associated" whereby they renounced all claim to personal profits and proceeded to distribute the profits arising from the beer sales pursuant to the undertaking given the citizens' meeting.

In assessing the respondent for the taxation year 1956 the Minister added to the respondent's declared income an amount deemed to have been his share of the partnership profits. The respondent's appeal from the assessment was allowed by the Tax Appeal Board and from that decision the Minister appealed to this Court.

Held: That as it was established by the evidence that the respondent did not receive and had no legal right to claim any of the profits arising from the sale of beer, the provisions of ss. 6(*c*) and 15 of the *Income Tax Act* had no application.

2. That as the partnership was a charitable organization as defined by s. 62(1)(*e*) and a non-profit corporation as defined by s. 62(1)(*f*) of the Act, its income was exempt from taxation.

APPEAL from a decision of the Tax Appeal Board[1].

The appeal was heard before the Honourable Mr. Justice Dumoulin at Quebec.

[1] (1960) 60 D.T.C. 257; 24 Tax A.B.C. 161.

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Maurice Paquin, Q.C. and *Roger Tassé* for appellant.

Pierre Letarte, Q.C. and *Julien Chouinard* for respondent.

DUMOULIN J. now (February 22, 1962) delivered the following judgment:

Le Ministre du Revenu national défère à cette Cour une décision de la Commission d'appel de l'impôt, en date du 15 décembre 1959, qui maintenait un pourvoi relatif à la cotisation de Charles-Auguste Bégin, de la cité de Mont-Joli, province de Québec, pour l'année d'imposition 1956.

L'instruction et la décision de cet appel ont été de consentement rendus applicables à une cause connexe et identique, celle du Ministre du Revenu national et Louis-Joseph Gagnon, c.r., inscrite sous le numéro 161421 des registres de cette Cour.

M. Charles-Auguste Bégin établissait son revenu réel, pour l'année 1956, à la somme de $3,705.77.

Le 20 février 1958, le Ministère du Revenu national avisait M. Bégin qu'une cotisation révisée majorait le chiffre de son revenu pour 1956, soit $3,705.77 à celui de $20,337.67.

L'addition litigieuse porte sur un poste de $16,556.90 que l'intimé avait omis dans son rapport d'impôt, pour les motifs relatés aux articles 1 à 7 de la réponse à l'avis d'appel, que je m'efforcerai de résumer.

En 1949, un référendum fut tenu à Mont-Joli pour connaître l'opinion de la population locale sur la question de la vente de la bière dans les limites de cette municipalité.

A la très faible majorité de 7 votes, les anti-prohibitionistes l'emportèrent, mais leurs adversaires ne désarmèrent pour autant. De longs pourparlers entre les deux groupes aboutirent à un compromis assez original.

Un fort groupe de citoyens représentatifs, de Mont-Joli, comprenant le maire, les échevins, le président de la Chambre de commerce, les membres de la ligue d'action civique, puis, ce corps, austère entre tous, la société Saint-Jean-Baptiste, et enfin l'association sportive de Mont-Joli, convinrent de régler le problème en obtenant un permis pour la vente de la bière au profit des œuvres de charité et de bienfaisance de la municipalité. Des bourses d'études, des subventions aux centres de loisirs et aux organisations de culture physique étaient également au nombre des objectifs prévus.

Dans la poursuite de ces fins méritoires, une assemblée fut tenue, le 2 novembre 1949, au sanatorium Saint-Georges de Mont-Joli, réunion à laquelle assistaient les notables ci-haut mentionnés, ainsi que M. Georges-Henri DeChamplain qui, en cette occasion, représentait le curé de la ville.

Entre autres décisions, il fut alors arrêté que (Mémorandum, pièce A-1):

1. Un accord définitif devra être fait avec la Commission des Liqueurs de Québec (par l'entremise et avec l'aide de l'Honorable Onésime Gagnon, député du comté, si nécessaire), dans le but d'obtenir l'assurance que cette Commission n'émettra qu'une seule licence pour la vente de la bière dans les limites de la ville de Mont-Joli et que la dite licence sera émise, conformément aux désirs de cette assemblée, en faveur d'une personne qui renoncera à l'exploiter pour son profit personnel et s'en servira à la fin exclusive de créer des fonds qui devront être distribués pour fins de bienfaisance, d'éducation, d'œuvres sociales, sous forme de bourses d'études, organisation des loisirs et des sports, aide aux divers corps publics dans le but du développement et de l'embellissement de Mont-Joli.

Un second article stipulait la création «sous forme de société civile de bienfaisance et de philanthropie», d'un organisme chargé d'exploiter le permis de vente de la bière et de veiller au contrôle et à la distribution des profits éventuels.

L'article 3 particularise l'emploi des fonds ainsi réalisés, et je cite:

3. Les argents obtenus par cet organisme seront employés d'abord à l'octroi de bourses d'étude pour aider les étudiants de Mont-Joli et favoriser l'éducation et l'instruction de jeunes gens qui seront susceptibles de contribuer dans l'avenir au développement de notre ville, et au moins un tiers environ des dits profits devront être employés à cette fin. Une autre part substantielle des argents à être réalisés devront être employés aussi à l'organisation des loisirs pour la jeunesse, à la création d'associations sportives ou à la subvention des associations déjà existantes dans la localité, dans le but de favoriser la pratique des sports parmi la jeunesse ainsi que de lui assurer des loisirs utiles à sa formation. Le surplus des profits réalisé devra être employé et distribué au profit des œuvres civiques et sociales ainsi que pour aider au développement et à l'embellissement de la ville de Mont-Joli.

Nous lisons à la fin de l'article 4 de ce Mémorandum, produit sous la cote A-1, que «. . . M. Charles-A. Bégin, négociant à Mont-Joli, est désigné et recommandé par la dite assemblée pour obtenir à son nom le dit permis et pour former avec les deux autres ci-dessus désignés l'organisme qui aura charge d'exécuter les vues et les desiderata de l'assemblée ci-dessus exprimés».

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Dumoulin J.

L'indubitable intention que les véritables exploitants de ce négoce philanthropique seraient les organismes et associations déjà nommés ressort en maints passages du Mémorandum, et je n'en rapporterai qu'un exemple extrait des premières lignes du paragraphe 5.

> Dans le but d'aider les mandataires de la dite assemblée dans la distribution selon les fins ci-dessus exposées, des profits réalisés et des argents obtenus pour l'avantage de la collectivité dont ils sont constitués les fiduciaires, un organisme supplémentaire devra être créé, comprenant les principaux citoyens de Mont-Joli et autant que possible, les représentants des diverses associations de la localité . . .

A l'occasion de cette même délibération, Me Louis-Joseph Gagnon, c.r., depuis Juge de la Cour de Magistrat de district, et Monsieur A.-H. Boudreau, saisirent les assistants du résultat de leur démarche auprès des autorités de la Commission des Liqueurs à Québec. Messieurs Gagnon et Boudreau firent part de l'acquiescement de la Commission des Liqueurs à n'émettre qu'un seul permis pour la vente de la bière à Mont-Joli, à cette réserve près, que ce privilège ne pouvait être accordé à une association, mais nommément à une personne désignée, qui «pourra l'opérer ou la faire opérer par une association créée pour des objectifs de bienfaisance et de charité sans but de gain ou de profit pour les associés», comme on l'a vu à la première page du Mémorandum.

Le 20 avril 1949, conformément aux résolutions arrêtées, le 2 du même mois, Messieurs A.-H. Boudreau, C.-A. Bégin et Me L.-J. Gagnon rédigèrent un acte intitulé: CONVENTION DE SOCIÉTÉ, ici produit sous la cote A-1, comme pièce annexe du Mémorandum.

Ce document, dès sa toute première ligne, précise que «pour se conformer au mandat qui leur a été confié par une assemblée de représentants des diverses associations, corps publics et principaux notables de Mont-Joli, tenue au sanatorium Saint-Georges, le 2 avril 1949», messieurs Bégin, Gagnon et Boudreau:

> . . . . déclarent s'associer ensemble dans un but de bienfaisance et de philanthropie, sous la raison sociale de "Les Distributeurs Associés", pour la distribution des profits d'une licence de bière, qui sera obtenue par l'un des associés pour la vente de la bière à Mont-Joli, en vertu d'un permis de la Commission des Liqueurs de la Province de Québec, accordé pour la réalisation des fins ci-après exprimées.

Il est entendu que la dite Association est faite sans aucun esprit de gains ou de revenus pour aucun des associés et que ceux-ci ne pourront, sous aucune forme que ce soit, retirer personnellement, retenir ou de quelque façon s'approprier aucune des sommes à distribuer et provenant du surplus des ventes de bière autorisées par le permis, lesquels surplus devront tous être distribués par les dits associés, pour fins de bienfaisance, charité, éducation, aide aux étudiants pauvres, œuvres sociales et civiques, organisation des loisirs pour la jeunesse, aide aux Corporations Scolaires et Municipales de Mont-Joli, pour les mêmes fins, ceux-ci agissant à ces fins comme fiduciaires de la collectivité.

Remarquons d'abord les qualités de mandataires et de fiduciaires expressément assumées par les trois prête-noms. Il importe également de noter une double admission faite par le savant procureur de l'appelant, Me Maurice Paquin, c.r. Je reproduirai ces deux passages qui apparaissent respectivement aux pages 72 et 85 de la transcription des témoignages devant la Commission d'appel de l'impôt. Cette transcription fut, de consentement, versée au dossier de l'appel.

A la page 72, Me Paquin s'exprime en ces termes:

D'ailleurs, le débat, monsieur le Président, et je tiens à le dire tout de suite, ce n'est pas sur cette question de savoir si messieurs Gagnon, Bégin et Boudreau ont retiré personnellement quelque argent de ça. Ce n'est peut-être pas admis de la façon que mes adversaires aimeraient que je l'admette, mais, éventuellement, il ne leur est rien resté de ça.

A la page 85, à cette assertion de Me Pierre Letarte, c.r., procureur de Messieurs Bégin et Gagnon:

Maintenant, demandons-nous ce qui s'est passé dans la réalité. Je pense qu'il va falloir admettre de part et d'autre que personne des trois personnes concernées n'a touché un seul cent de cette affaire-là. Je pense que ç'a été bien établi à la fois par les témoins et par les documents, et mon savant confrère de l'Impôt admettra probablement la même chose.

Me Paquin répondra laconiquement mais de façon concluante: «D'accord».

Je me sens donc dispensé de reproduire les déclarations des témoins puisque, je le redirai une fois pour toutes, ni M. Bégin, ni Me Gagnon, n'ont touché un seul sou des profits provenant de ce débit de bière.

Le litige se situera désormais sur le plan du droit, sans autre référence aux incidents matériels.

Le Ministère du Revenu national, à l'article 7 de son avis d'appel, soumet que:

7. ... Messieurs Louis-Joseph Gagnon, Alfred H. Boudreau et Charles-Auguste Bégin, faisant affaires en société sous les nom et raison sociale de "Les Distributeurs Associés de Mont-Joli", opéraient un commerce de

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vente de bière, au cours de l'année d'imposition 1956, ce qui constitue une entreprise au sens des dispositions de l'article 139(1)(*e*) de la Loi de l'impôt sur le revenu et qu'en conséquence, le bénéfice annuel qui découle de telle entreprise est assujetti aux dispositions des articles 3 et 4 de ladite loi.

Dumoulin J.

L'appelant se base sur les articles 3, 4, 6(*c*), 15(1), 62(1)(*e*), 62(1)(i) et 139(1)(*e*) de la Loi de l'Impôt sur le revenu, puis sur les articles 1830 à 1900, inclusivement, du Code civil de la province de Québec.

Par contre, le plaidoyer de défense de l'intimé énonce que les trois sociétaires, sous la raison sociale de «Les Distributeurs Associés, enrg», n'ont fait que se rendre au désir de la population de Mont-Joli, dont ils ont accepté un mandat collectif, dans un but social, charitable, à titre purement bénévole. Ces trois particuliers, continue la réponse à l'avis d'appel, ne prétendent et n'ont aucun droit au revenu du permis de débit de bière, octroyé au nom de l'un d'eux, (M. Bégin), pour l'avantage de la communauté. Aucun des associés n'a effectué de mise de fonds et nous avons entendu l'admission conjointe qu'aucun d'eux n'a retiré le moindre bénéfice ou émolument de l'entreprise. C'est pourquoi l'intimé conclut que les circonstances du cas actuel ne donnent pas ouverture aux articles 6(*c*) et 15, mais bien à la clause d'exception de l'article 62(1)(*i*) de la Loi de l'Impôt sur le revenu (S.R.C. 1942, c. 148).

Il a été dit que l'appelant fonde ses moyens de droit, entre autres, sur le titre XI du Code civil, celui de la Société. Sans méconnaître que le vocable de «société», selon l'acception du droit civil, suffirait à atteindre, le cas échéant, certaines associations, mais de nature lucrative, celles-là, je n'ai relevé qu'un seul passage digne de remarque, le second principe énoncé par l'article 1831:

> Toute convention par laquelle l'un des associés est exclu de la participation dans les profits est nulle.

Dans un contrat ordinaire de société, une telle clause disparaîtrait sans nécessairement invalider les autres dispositions. Mais dans le cas qui nous occupe, la gratuité absolue du mandat, nominalement accepté pour des fins de pure et simple philanthropie, se confond si intimement avec cette raison d'être de l'entreprise, qu'il me paraît impossible d'enlever cette condition sans annuler du même coup le projet tout entier. Chacun des trois distributeurs associés

s'est reconnu mandataire et fiduciaire d'organisations civiques; chacun a spécifiquement renoncé à tout espoir de gains personnels. Bien qu'il ne me soit pas nécessaire de préciser les recours légaux, susceptibles d'assurer le respect de tels engagements, je n'hésite pas à tenir que ces moyens coercitifs existaient.

La loi des compagnies de la province de Québec, au chapitre 276 des Statuts refondus de 1941, comporte spécifiquement en sa Troisième Partie, à l'article 214, la disposition ci-dessous:

> Le lieutenant-gouverneur peut, au moyen de lettres patentes, sous le grand sceau, accorder une charte à tout nombre de personnes, n'étant pas moindre que trois, qui demandent leur constitution en corporation sans intention de faire un gain pécuniaire, dans un but national, patriotique, religieux, philanthropique, charitable, scientifique, artistique, social, professionnel, athlétique ou sportif ou autre du même genre.

La lecture de l'article 215, plus particulièrement celle de l'alinéa (*d*) portant que la requête réglementaire indiquera «le montant auquel sont limités les biens immobiliers ou les revenus en provenant, que peut acquérir et posséder la corporation», permet d'inférer que la réalisation de profits n'est pas interdite à ces corporations ou associations, pour des fins bénévoles, sociales ou culturelles. L'entité légale fut conférée aux «Distributeurs Associés» conformément aux dispositions de cette troisième partie de la loi des compagnies.

Les états financiers de l'Association, dressés par la maison de comptabilité McDonald, Currie & Co., révèlent de très importantes distributions d'argent aux sociétés civiques et autres, que l'on pourrait dire les véritables commanditaires, sans toutefois attacher à ce qualificatif le sens technique que lui confèrent les articles 1871 et 1872 du Code civil. Les bilans déposés au dossier, sous les cotes A-3, A-4 et A-5, fournissent toutes les précisions requises à cet égard. Quant à la gestion du débit de bière, elle relevait de l'employé nécessairement salarié, monsieur Ludger Ouellette, assisté d'un comptable, monsieur Charles-Auguste Gagnon.

Passons maintenant à l'étude des articles de la Loi de l'Impôt sur le revenu sur lesquels les litigants ont basé leurs prétentions contradictoires. Il est assez rare que les parties se réclament de textes identiques pour en inférer des solutions dissemblables. En pareil cas, le critère d'appréciation résultera de l'interprétation des faits.

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L'intimé Bégin, comme à plusieurs reprises, nous l'avons constaté, n'a rien reçu, ni ne pouvait rien recevoir de sa participation officieuse à l'initiative de bienfaisance, dont les «Distributeurs Associés» n'ont été qu'une émanation organique.

Cela étant, comment pourrait-on lui appliquer, pour l'année d'imposition 1956, les directives édictées à l'article 6 de la Loi de l'Impôt sur le revenu et à son alinéa (*c*):

> 6. Sans restreindre la généralité de l'article 3, doivent être inclus dans le calcul du revenu d'un contribuable pour une année d'imposition
>
> *c*) le revenu que le contribuable a tiré d'une société ou d'un syndicat pour l'année, qu'il l'ait touché ou non pendant l'année.

Même commentaire à l'égard de l'article 15, puisque M. Bégin ne fut ni un associé réel et moins encore le propriétaire d'une société ou entreprise commerciale selon le sens juridique et usuel du terme.

A mon avis, la disposition décisoire, en l'occurence, se trouve à l'article 62(1) et à ses sous-paragraphes (*e*) et (*i*), dont voici la teneur:

> 62. (1) Aucun impôt n'est exigible en vertu de la présente Partie . . .
>
> (*e*) d'une organisation de charité constituée en corporation ou non, dont toutes les ressources étaient consacrées à des œuvres de bienfaisance exercées par ladite organisation et dont aucune partie du revenu n'était payable à un propriétaire, membre ou actionnaire de ladite organisation, ou par ailleurs mise à sa disposition pour son avantage personnel.
>
> (*i*) d'un club, une société ou association organisée et fonctionnant uniquement pour des fins de bien-être social, améliorations civiques, plaisirs, récréation ou pour quelque autre fin non rémunératrice, dont aucune partie du revenu n'était payable à un propriétaire, membre ou actionnaire des susdits, ou par ailleurs mise à sa disposition pour son avantage personnel.

Je crois, en effet, que ces exemptions favorisaient expressément des entités sociales ou autres du genre de celle dont il s'agit actuellement. Il me semble inouï, expression plutôt euphémique, d'accoler à l'intimé un prétendu revenu de $16,556.90 dont il n'a pas même eu un denier, revenu, je le répète, qu'il n'avait aucun droit d'exiger de l'association des Distributeurs enregistrés.

Telle est l'interprétation que des conjonctures comparables ont suggéré au président de cette Cour, l'honorable Juge Thorson, dans les causes de *Kenneth B. S. Robertson Limited v. The Minister of National Revenue*[1] et *St.*

[1] [1944] Ex. C.R. 170.

Catharines Flying Training School Limited v. The Minister of National Revenue[1]. Le statut applicable dans ces deux instances était celui des revenus de guerre (S.R.C. 1927, c. 97), de même teneur que la Loi de l'Impôt sur le revenu, texte de 1948.

Dans la première instance, il fut décidé que:

> . . . where an amount is paid as a deposit by way of security for the performance of a contract and held as such, it cannot be regarded as profit or gain to the holder until the circumstances under which it may be retained by him to his own use have arisen and, until such time, it is not taxable income in his hands, for it lacks the essential quality of income, namely, that the recipient should have an absolute right to it and be under no restriction, contractual or otherwise, as to its disposition, use or enjoyment.

La seconde se rapproche davantage de celle actuellement à l'étude. La partie appelante avait obtenu l'existence sociale selon la partie première de la Loi des compagnies du Canada, 1934, avec pouvoir de maintenir une école élémentaire d'aviation, où pourraient s'entraîner des apprentis-pilotes, sous l'égide du «British Commonwealth Air Training Plan». Cet organisme ne devait distribuer ni dividende, ni profit pendant la durée de son contrat. Une prolongation de vie corporative fut consentie avec stipulation que les gains éventuels seraient dorénavant versés à un club aéronautique reconnu par le Ministère de la Défense nationale, ou payés à la Couronne.

Si étrange que cela puisse paraître, l'État prétendit prélever une taxe sur les bénéfices de ce club d'aviation pour les périodes comprises entre 1941 et 1945. La décision de la Cour fut la suivante:

> *Held:* That the term "association" in its ordinary meaning is wide enough to include an incorporated company and does not exclude an incorporated company such as the appellant.
>
> 2. That the purposes referred to in the term "non-profitable purposes" as used in section 4(*h*) are purposes that are carried out without the motive or intention of making a profit, that is to say, purposes other than that of profit making.
>
> 3. That the appellant was an association that was organized and operated solely for non-profitable purposes within the meaning of section 4(*h*).
>
> 4. That no part of the appellant's income inured to the benefit of any of its stockholders or members.

[1] [1953] Ex. C.R. 259.

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Ce jugement mettait en pratique l'article 4 et ses sous-paragraphes (*h*) et (*e*) de la Loi des revenus de guerre (S.R.C. 1927, c. 97).

> 4. The following incomes shall not be liable to taxation hereunder:—
>
> (*h*) The income of clubs, societies and associations organized and operated solely for social welfare, civic improvement, pleasure, recreation or other non-profitable purposes, no part of the income of which inures to the benefit of any stockholder or member;
>
> (*e*) The income of any religious, charitable, agricultural and educational institution, board of trade and chamber of commerce, no part of the income of which inures to the personal profit of, or is paid or payable to any proprietor thereof or shareholder therein.

La similitude de cette disposition légale avec le libellé de l'article 62(1)(*e*) et (*i*) de la Loi de l'Impôt sur le revenu est manifeste.

En matière d'impôt, une sage doctrine veut que toute mesure fiscale ait une signification littérale, excluant tout tempérament d'équité. Autrement dit, le texte de loi, selon le mot à mot de sa rédaction, fait foi de la pertinence de la taxe.

Je rapporterai deux exemples de cette jurisprudence toujours suivie.

Dans *Ormond Investment Co. Ltd. v. Betts*[1] (H.M. Inspector of Taxes), Lord Atkinson disait:

> . . . it is well established that one is bound in construing Revenue Acts to give a fair and reasonable construction to their language without leaning to one side or the other, that no tax can be imposed on a subject by an Act of Parliament without words in it clearly showing an intention to lay the burden upon him, that the words of the Statute must be adhered to and that so-called equitable constructions of them are not permissible.

Et encore, dans *The Cape Brandy Syndicate v. C.I.R.*[2], le Juge Rowlatt décrétait:

> . . . in taxation you have to look simply at what is clearly said. There is no room for any intendment; there is no equity about a tax: there is no presumption as to a tax; you read nothing in; you imply nothing, but you look fairly at what is said and at what is said clearly and that is the tax.

Pour tous ces motifs, je suis d'avis que l'appelant n'a pas prouvé ses moyens d'appel et que l'intimé, par ailleurs, a justifié l'admissibilité de sa défense.

[1] 13 T.C. 400-434.

[2] 12 T.C. 358-366.

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En conséquence, la Cour décrète que l'appel doit être rejeté et le dossier retourné au Ministère du revenu national afin d'enlever un montant de $16,556.90 du revenu réel de l'intimé pour l'année d'imposition 1956, et qu'une nouvelle cotisation, conforme à ce jugement, soit subséquemment émise.

L'intimé aura droit de recouvrer tous ses dépens après taxation.

Jugement conforme.

BETWEEN:

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Jan. 22

Feb. 26

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

AND

BONAVENTURE INVESTMENT COMPANY LIMITED ..... RESPONDENT.

Revenue—Income tax—Payment in settlement of claim for breach of option to convey lots to builder—Capital or income receipt—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4 and 139(1)(e).

The respondent, whose business was the building of houses for sale, purchased fifty building lots from a syndicate and secured an option to purchase fifty more lots at the same price. The vendor subsequently refused to honour the option but on threat of suit paid the respondent $7,500 in settlement of its claim. In re-assessing the respondent for its 1956 taxation year the Minister added $7,500 to its taxable income. The respondent appealed from the assessment on the ground that the payment constituted non-taxable compensation for damages of a capital nature which should not have been treated as income. The Tax Appeal Board allowed the appeal. On an appeal by the Minister from the decision of the Board.

Held: That the building lots in question formed part of the respondent's stock in trade and the payment of $7,500 was to compensate it for the loss of business profits and therefore was properly included in computing its taxable income. *Burmah Steam Ship Co. Ltd. v. Commissioners of Inland Revenue* 16 T.C. 67 at 71, and *Jesse Robinson & Sons v. Commissioners of Inland Revenue* 12 R.T.C. 1241 at 1247, referred to.

APPEAL from a decision of the Tax Appeal Board[1].

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

[1] (1960) 23 Tax A.B.C. 408; 60 D.T.C. 136.

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MINISTER OF NATIONAL REVENUE v. BONAVENTURE INVESTMENT CO. LTD.

Paul Boivin, Q.C. and *Rolland Boudreau* for appellant.

Mitchell Klein for respondent.

DUMOULIN J. now (February 26, 1962) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board, on date February 25, 1960[1], annulling a reassessment by the Minister of National Revenue, whereby an amount of $7,500 was added to respondent's taxable income for the year 1956.

The facts giving rise to this litigation are uncontradicted and quite simple.

Bonaventure Investment Co., Ltd., is described by its secretary-treasurer, Mr. Bernard Lazarowitz, as a "construction company . . . buying some farms for a bigger amount of land, and . . . building it up (cf. transcript of evidence before Tax Appeal Board, pp. 4-9)". The respondent's income tax return, for the fiscal period ended March 31, 1956, (photostats filed as ex. R-1), states the nature of this company's business under the caption of "real estate and builders".

It began operating at the start of 1953, says Mr. Lazarowitz, so that this firm had existed no longer than six or seven months when, on July 24 of that same year, it . . . "offered to purchase from Messrs. Morris Schwartz, Harry Finestein and David Miller, fifty building lots forming part of lots 9 and 10, Parish of Lachine, Town of Dorval."

The second paragraph of this offer (ex. A-1) reads thus:

> In addition you (i.e. Messrs. Schwartz, Finestein and Miller) agree to give us an option to purchase an additional (50) fifty lots out of the same parcel of land and of the same approximate area at the same price; such offer to be exercised by the undersigned in writing within a period of four (4) months after date of execution of your Deed of Sale for the purchase of the entire parcel of land.

Another paragraph, the third of this private agreement, proposed an over-all price of . . . "One Hundred and Fifty Dollars ($150.00) per lot above your costs for each lot . . .".

A few days after, on August 10, Morris Schwartz inscribed on this document (ex. A-1) the significant words: "Offer hereby accepted", under which appears his sign-manual.

No complications occurred in connection with the first block of 50 lots bought outright, legal ownership of which was regularly delivered to Bonaventure Investment, this company then proceeding to build 50 bungalows and disposing of the entire development.

Matters, however, turned out differently in the case of the parcel under option, quibbles and misunderstandings set in to such an extent that both parties threatened a recourse to legal redress. Eventually an amicable settlement of the dispute was decided upon, as evidenced in ex. A-8, merely dated 1955, intituled: "Memorandum of Agreement", whereby Schwartz, Finestein and Miller, undertook to pay $7,500 to Bonaventure Investment Ltd., without any admission of liability, but solely to "settle and transact their respective claims" with respect to the option aforesaid. This sum of $7,500, and that alone constitutes the moot point under discussion. In respondent's opinion, as appears in section 4 of its Reply to Notice of Appeal:

> 4. The amount at issue received by the Respondent constituted non-taxable compensation for damages and are of a capital nature.

To this proposition, the appellant replies that (cf. Notice of Appeal, section 17):

> 17. The building lots in question formed part of the stock in trade of the Respondent, and, in the same way as the profits from the disposal of these lots would have been income in the hands of the Respondent, the compensation received in lieu of such profits is likewise income taxable in the hands of the Respondent.

Accordingly, the appellant relies on sections 3, 4 and 139(1)(*e*) of the *Income Tax Act* (1952, R.S.C. c. 148).

Capital increment or trading receipt, then is the problem calling for a solution.

A first question logically coming to one's mind is the true nature of the commercial transactions carried on, normally, by Bonaventure Investment. In other words, whenever this "builders and real estate" company sold one or several lots, with house thereon, was it parcelling off so many capital assets or simply plying its regular line of activities and dealing, for an adequate consideration, with its stock in trade? The answer seems unescapable, and if I may be permitted such expressions in reference to real property, the respondent's "wares" his one and only kind of "inventory goods" consisted in land holdings. Erection of cottages on these grounds just superimposed, on the plots of real estate, a

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second profit earning item and nothing else. I mention this in reply to respondent's assumption that its uniform practice of dealing only in built-up lots and not in resales of bare land (cf. transcript p. 10) might have some legal bearing on the issue. And again, it could go without saying that the company's gains have a twofold basis, computed on a percentage of its purchase price of the soil and on subsequent construction costs.

In consequence of a breach of contract the respondent company was restricted in the exercise of its trade, failing to obtain delivery of fifty (50) "inventory assets", and obtained, as a compensation, a sum of $7,500. Admittedly the current expression of "compensatory damages" aptly qualifies such a payment.

Even so a second question arises, namely: Were these "compensatory damages" granted "to fill a hole in respondent's capital assets or rather a hole in its commercial profits?" as said in *Burmah Steam Ship Co., Ltd. v. C.I.R.*[1]

The company's purpose, its one and only interest in the option, was to transact the sales of those fifty lots immediately after the building of so many cottages; it never intended any long term retention of this property which alone might, in time, impart to the deal a characteristic feature of an investment. To a curtailment of trading profits corresponded an indemnity of a like nature, with the result that Bonaventure Investment derived a certain amount of pecuniary benefits from a single source instead of from a possible fifty. Therefore, appellant's suggestion that: "the building lots in question formed part of the stock in trade . . . and the compensation received in lieu of such profits is likewise income taxable in the hands of the respondent", seems fully vindicated.

Out of several precedents quoted, two are of particular assistance: Referring anew to the *Burmah* case, *supra*, the undergoing statement made by Lord President Clyde singles out an instance of differentiation between profits of trade and a capital gain.

> Suppose some one who chartered one of the Appellant's vessels breached the charter and exposed himself to a claim of damages at the Appellant's instance, there could, I imagine, be no doubt that the damages recovered would properly enter the Appellant's profit and loss account for the year. The reason would be that the breach of the charter was an injury inflicted on the Appellant's trading, making (so to speak) a

[1] (1930) 16 T.C. 67 at 72.

hole in the Appellant's profits and the damage recovered could not therefore be reasonably or appropriately put by the Appellant—in accordance with the principles of sound commercial accounting—to any other purpose than to fill that hole. Suppose, on the other hand, that one of the Appellant's vessels was negligently run down and sunk by a vessel belonging to some other shipowner, and the Appellant recovered as damages the value of the sunken vessel, I imagine that there could be no doubt that the damage so recovered could not enter the Appellant's profit and loss account because the destruction of the vessel would be an injury inflicted, not in the Appellant's trading, but on the capital assets of the Appellant's trade, making (so to speak) a hole in them, and the damages could therefore—on the same principle as before—only be used to fill *that* hole.

More in line still with the issue at bar was a pronouncement by Rowlatt J. in re: *Jesse Robinson & Sons v. The Commissioners of Inland Revenue*[1]. There, the following facts had engendered the litigation as reported at pages 1241 and 1242:

> On 17th March, 1920, the Appellants entered into a contract to sell a quantity of yarn at a specified price. On 21st June, 1921, they agreed with the purchaser to cancel the uncompleted portion of the contract upon payment by the purchaser of a sum of £200 in four monthly instalments, . . .
>
> On 29th August, 1919, and 15th March, 1920, the Appellants entered into contracts for the sale of certain quantities of yarn at specified prices. On 19th July, 1920, the purchaser wrote to the Appellants purporting to cancel the first contract so far as it was unperformed and purporting wholly to cancel the second contract. On 16th June, 1921, the purchaser agreed to pay to the Appellants £12,500 in settlement of their claim for damages for breach of contract. The said sum was paid on the 18th June, 1921.
>
> In computing the profits of the Appellants for the accounting period of one year . . . the Commissioners of Inland Revenue treated the said sums of £200 and £12,500 as trading receipts of that period.

On appeal of this decision to the High Court of Justice, the learned Judge took the view that:

> . . . there was a broken contract, and an action was commenced in respect of it, and the action was settled by payment of damages for breach of contract. It seems to me that there is no reason why the sum received in that respect for breach of contract is not a sum which is part of the receipts of the business for which that contract was made.

Notwithstanding any legal distinctions attaching to chattels (yarn) and real property (residential lots), an admissible analogy exists between the *Jesse Robinson* precedent and the instant case. Indeed, a decisive factor arises, not so much out of the species of things sold, moveable or immoveable, as from the transaction (commercial or otherwise) in

[1] (1929) 12 R.T.C. 1241 at 1247.

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the course of which the sale occurs. I renew my conviction that this payment of $7,500 to Bonaventure Investment Co., Ltd., compensated it for the loss of business profits, and, therefore, ranges such a receipt well within the compass of ss. 3 and 4 of the *Income Tax Act*.

For the reasons previously given, the appeal is allowed and respondent's assessment restored, as of May 22, 1958, when appellant, by notice of assessment, included the amount of $7,500 in the taxable income of Bonaventure Investment Company Ltd., for taxation year 1956.

The appellant is entitled to recover its costs after taxation.

Judgment accordingly.

1960

Oct. 6, 7, 11, 12

1962

Mar. 21

BETWEEN:

PARSONS-STEINER LIMITED .....APPELLANT;

AND

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

Revenue—Income—Income tax—Compensation received by agent for loss of agency—Capital receipt or income.

The appellant company was incorporated in 1930 to carry on the business of a manufacturer's agent and wholesale merchant dealing in china and related wares. From its inception the appellant represented the manufacturers of the Royal Albert line of tea ware and in 1933 became sole agent in Canada for the sale of dinner, tea and toilet ware and ornamental and other goods manufactured by Doulton & Co. Ltd. The two agencies were the principal ones which the appellant operated and accounted for 80% of its business. As exclusive agent for Doulton & Co. Ltd., the appellant was remunerated by a commission on all sales in Canada whether the order was secured by it or placed directly by the customer. The Doulton products sold by the appellant consisted principally of dinnerware and figurines and there was no competition between these lines of goods and the other lines the appellant sold.

The agency agreement between the appellant and Doulton & Co. Ltd., provided that it should remain in force for one year from March 31, 1933, and it was determinable upon three months notice given by either party. The agency in fact was continued to December 31, 1955 and was not terminated by notice but by an agreement made early in 1954 which culminated negotiations begun some time previously when the English company decided to set up a Canadian sales subsidiary.

Pursuant to the agreement terminating the agency, Doulton & Co. Ltd. paid the appellant $100,000 "in full settlement of your claim for damages for loss of rights under the agreement".

In re-assessing the appellant for the 1956 taxation year the Minister added this payment to the appellant's declared income. In an appeal from the assessment the appellant, while admitting that $5,000 of the amount was income, contended that the remainder was capital.

Held: That, except in so far as it was a consideration for services rendered to Doulton & Co. Ltd. in connection with the take-over by its subsidiary, which is admitted to be income, and except in so far as it took the place of commissions on sales of goods ordered before, but invoiced after December 31, 1955, the payment was not income from the appellant's business but was referable to the appellant's claim for loss of what it and Doulton & Co Ltd. considered to be the appellant's interest in the goodwill and business in Doulton products in Canada.

2. That this was a capital asset of an enduring nature and the payment received in respect of its loss was accordingly a capital receipt.

Wiseburgh v. Domville [1956] 1 All E.R. 754 at 757,760; *Commissioners of Inland Revenue v. Fleming & Co. (Machinery) Ltd.* 33 T.C. 57 at 61, referred to.

APPEAL under the *Income Tax Act.*

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

H. H. Stikeman, Q.C. and *P. N. Thorsteinsson* for appellant.

G. W. Ainslie for respondent.

THURLOW J. now (March 21, 1962) delivered the following judgment:

This is an appeal from a re-assessment of income tax for the year 1956, the issue between the parties being whether the whole of a sum of $100,000 received by the appellant from Doulton & Co. Limited in that year following the termination of an agency relationship was income from the appellant's business. The appellant admits that $5,000 of the amount in question was income but contends that the remainder of it was capital.

The appellant was incorporated in 1930 and since then has carried on business on a considerable scale as a manufacturer's agent and as a wholesale merchant dealing in china and related wares. From the commencement of its operations the appellant represented the manufacturers of the Royal Albert line of tea ware and in 1933 it became the sole agent in Canada for the sale of dinner, tea and toilet ware and ornamental and other goods, manufactured

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PARSONS-STEINER LTD. v. MINISTER OF NATIONAL REVENUE

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by Doulton & Co. Limited. These two agencies were the principal ones under which the appellant subsequently operated and they accounted for approximately 80% of its business but several other agencies of minor importance were acquired from time to time and some of these were discontinued or terminated during the period from the incorporation of the company to the end of 1955.

As exclusive agent in Canada for Doulton & Co. Limited, the appellant sold goods of its principal's manufacture to buyers of large quantities on the principal's account and was remunerated by a commission on all sales made in Canada whether the order was secured by the appellant or was placed directly by the customer. But the appellant also purchased Doulton goods on its own account for sale as a wholesaler to smaller customers. Though tea ware is mentioned in the agency contract, the Doulton products sold by the appellant consisted principally of dinner ware and figurines and there was no competition between these lines of goods and the Royal Albert or other lines which the appellant sold. Moreover, while there were other lines of figurines on the market some of which were of finer quality and more expensive while others were of lower grade and not so expensive, the Doulton figurines, which accounted in the last two or three years to about 55% of the appellant's sales of Doulton products, were in a class by themselves in which there was no real competition from those of other makers.

The agency agreement between the appellant and Doulton Co. Limited provided that it should remain in force for one year, from March 31, 1933 and thereafter until determined by a three months notice which might be given by either party. In fact, the relationship continued until December 31, 1955, when it terminated pursuant to an agreement between the parties rather than pursuant to a notice of the kind mentioned in the agreement.

The appellant's sales—other than those for which it received commission—in the last four years of the relationship and the four following years and the commissions earned in the same years were as follows, the years being fiscal years of the appellant ending on June 30 in each year.

Year	*Sales*	*Doulton sales only*	*Commissions*
1952	1,051,000	671,000	176,000
1953	825,000	417,000	162,000
1954	777,000	328,000	134,000
1955	844,000	404,000	144,000
1956*	729,000	(no figure given)	151,000
1957	509,000		98,000
1958	474,000		84,000
1959	546,000		113,000

During 1953 correspondence passed between the appellant and Doulton & Co. Limited from which it appears that the latter was contemplating termination of the agency and early in 1954 a representative of that company came to Canada where discussions on that subject took place between him and the President of the appellant company. The situation which this presented from the point of view of the appellant appears from two letters written on behalf of the appellant to the representative of Doulton & Co. Limited at or about that time, the first dated January 18, 1954, and the second January 26, 1954, which I shall quote in full:

Mr. K. Warrington,
Doulton & Co. Limited,

Dear Ken:

It is our understanding that Doulton Limited are desirous of terminating their present Canadian agency arrangements, and establishing a wholly-owned subsidiary to represent their factories in this market.

Our firm naturally learns of this decision with considerable regret. Not only have we and Doulton become synonymous in the Canadian chinaware trade, but the happy and successful association of over twenty years duration is not lightly put aside. Because of the personal pride in your products which the principals of our firm have always felt, the Doulton side of our business has had pre-eminent consideration in our sales efforts, and consequently the results rival in volume the total business of all our other agencies combined.

It appears to us, however, that all our discussions concerning a fair and equitable settlement on which this "take-over" is to be based, is largely a matter of arriving at a valuation acceptable to us both of an established earning power, which we are giving up, and which will henceforth accrue to you.

This is not just a figure to be pulled out of the air. Negotiations based on such "horseback" appraisals seldom have a happy outcome. Accordingly, we have compiled the earnings figures (see exhibit attached) from our records, to try and determine a value for the Doulton side of our

*1956 includes six months of the Doulton agency and six months following its termination.

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business. You are no doubt able to verify these figures from your own records of Canadian sales and shipment, but we will be pleased to place our accounting records at your disposal, should you wish to verify them here.

It is apparent that our Canadian Doulton agency provides an average net earnings to Parsons-Steiner Limited of $75,000 per annum, after its proper share of our total overhead, and after deducting the corporation income tax applicable.

In arriving at the value of private businesses for purposes of sale, valuation, or assessment for inheritance taxes, the ratio of capitalizing in current use is 6⅔ to 8 times annual net earnings. Leaning your way (6⅔ times), this works out to a capitalized value of $500,000.

At this point in our calculation, we stopped and gave thoughtful consideration to the matter of how much of the successful development of the Doulton market in Canada has been a joint effort, in the sense that you as manufacturers had created an acceptable product, and that we have done a fine job of establishing and servicing a distribution organization which you can be proud to take over without modification.

In the light of this partnership aspect of our Canadian development, I personally have insisted that we split the above figure, 50-50%. This amount ($250,000) is the price of what we are discussing. You may be assured that in this price, there is included the continued goodwill and co-operation of this firm, and all its personnel, towards your new Canadian venture.

Sincerely,
President.

* * *

January 26, 1954.

Mr. J. K. Warrington,
Doulton & Co. Limited,
Royal Doulton Potteries,
Burslem, Stoke-on-Trent,
ENGLAND.

Dear Ken:

In the light of the discussions we have had together, since outlining our views to you in my letter of January 18th, we are prepared to modify our ideas.

Assuming that our present arrangements will continue as they are until December 31, 1954, we would feel compensated for the loss of our valued agency agreement with you at that time, if paid—

$175,000 either in cash *or* in the form of—

$175,000 par value 6% cumulative redeemable first preferred shares of Doulton (Canada) Limited

(or of whatever subsidiary Canadian company is incorporated to carry on here at that time).

These shares would carry the rights and privileges usually attached to preferred stock issues when created for sale to the public in Canada. They would be redeemable, all or in part, at the option of the issuing company

at 100% during 1955
at 101% during 1956
at 102% during 1957
at 103% during 1958
at 104% during 1959
or at 105% thereafter.

After 1956, a minimum of 10% of the original issue to be retired in each subsequent year by sinking fund at the prevailing call price.

As an optional plan, if you agree to extend our present agency arrangements a further year (to December 31, 1955) we would alter the above proposal to read

$100,000 in cash, or in said preferred shares.

It is our understanding that, at whatever take-over date is decided, we will be paid the commissions outstanding on business done between us as of that date; that you will buy, as well, our Doulton inventory at landed cost prices.

We agree to co-operate fully in your suggestion that one or two Doulton & Co Limited employees be associated with us here for any period prior to the take-over date. They will be given office accommodation, and every opportunity to familiarize themselves with the Doulton distributing aspect of our business.

Yours very truly,
PARSONS-STEINER LIMITED,
President.

Some time after these letters were written, Mr. Ernest Steiner, the President of the appellant and his son went to England where further discussions took place in which an agreement was reached and on April 29, 1954, Doulton & Co. Limited wrote to Mr. Steiner as follows:

Dear Mr. Steiner,

The subject of our recent conversations at Doulton House in connection with the ending of the Agency were submitted to the Board today and they have confirmed the proposition which we mutually agreed on Wednesday, 14th April. The sum of $100,000 will therefore be payable to your company subsequent to the termination of the Agency, this amount to include payment for such services as you will render in connection with our takeover of the Agency and also to take into account the fact that no commission will be payable to your company on goods invoiced after 31st December, 1955.

I hope to be in Toronto with Warrington in October and this will give us the opportunity to discuss with you the progress of the measures necessary to implement the agreement.

Yours sincerely,

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Pursuant to the arrangement so made the appellant continued to act as agent for Doulton & Co. Limited throughout the remainder of 1954 and the whole of the year 1955 and in the meantime afforded to Doulton & Co. Limited the office facilities and co-operation referred to for the purpose of facilitating the smooth transfer of the operation to its new Canadian subsidiary. Employees of Doulton & Co. Limited were accommodated by the appellant and its staff made a point of introducing such employees to customers who called at the appellant's place of business. The appellant pleads that these services were worth $5,000 and it is with respect to them that the appellant concedes that $5,000 of the $100,000 in question was income.

On the termination of the agency, two of the appellant's seventeen employees became employees of the Doulton subsidiary and thereafter orders addressed to the appellant for Doulton goods were referred to the Doulton subsidiary as the appellant no longer sold such goods even on its own account. In order to counteract the expected drop in sales the appellant employed several new salesmen and made a greater effort than formerly to augment sales of the lines which it still carried. There was no change made in the premises occupied by the appellant and no salaries were cut as a result of the loss of its Doulton agency. One new agency was obtained but no agency could be obtained for a line of figurines comparable with the Doulton line.

Payment of the $100,000 was forwarded early in 1956 with a letter which read as follows:

2nd January, 1956.

E. A. Steiner, Esq.,
Messrs. Parsons-Steiner Limited,
55-57 Wellington Street West,
Toronto 1, Canada.

Dear Mr. Steiner,

As arranged I have pleasure in enclosing my company's cheque for $100,000. As we do not admit liability we regard this sum as a voluntary gesture to maintain our good name in Canada and you have agreed on behalf of your company to accept it in full settlement of your company's claim for damages for loss of rights on the cancellation as at 31st December, 1955 of the agreement hitherto existing between our two companies.

A signed copy of this letter is enclosed: will you please sign and return the original to me as a receipt and acknowledgement that the agreement between the two companies is hereby cancelled as of 31st December, 1955 and that you accept the sum of $100,000 in full settlement of your claim for damages for the loss of rights under the agreement.

Yours sincerely,
Managing Director

Received from Doulton & Co. Limited the sum of $100,000 in accordance with the above terms.

This was acknowledged by a letter of January 4th, 1956, from the appellant to Mr. E. Basil Green of Doulton & Co. Limited which simply said:

Dear Mr. Green:

This is to acknowledge with thanks your cheque for $100,000.00 in respect to damages on termination of our contract.

Yours very truly,
PARSONS-STEINER LIMITED
E. A. Steiner.

The question to be determined is whether the $100,000 was profit from the appellant's business. If so, it is income in respect of which the appellant is liable to tax. If not, it is conceded that there is no basis for tax liability in respect to it.

So far as I am aware, there is no case of this kind reported in Canada but a number of cases in the Courts of England and Scotland were cited in the course of the argument. What appears most clearly from these cases is that the question is largely one of degree and depends on the facts of the particular case and the inferences to be drawn therefrom. For the purposes of this case the distinction drawn in the cases appears to me to be summed up in the following passage from the judgment of Lord Evershed, M.R., in *Wiseburgh v. Domville*[1]:

Was this sum paid by way of damages in respect of this agency contract "profits or gains" arising from the trade of the taxpayer as a sales agent? The argument of counsel for the taxpayer had the attraction of simplicity. He said the £4,000 was paid to the taxpayer in exchange for a profit-earning asset which he had lost owing to the breach of the contract by the company, and it followed that it was a capital item. If the question were res integra that argument would be more attractive still, but it clearly will not stand as a test in the light of the authorities. For the most part these authorities are decisions of the Inner House of the

[1] [1956] 1 All E.R. 754 at 757.

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Court of Session in Scotland which do not bind this court. But the Income Tax Acts apply indifferently on either side of the border, and I should be slow to adopt a new approach to the incidence of taxation in England from that established in Scotland. In other words, I feel we should follow the line of the Scottish decisions and the principle which can be extracted from them.

In *Kelsall Parsons & Co. v. Inland Revenue* (1938) (21 Tax Cas. 608), Lord Normand (Lord President), said (ibid., at p. 619):

". . . no infallible criterion emerges from a consideration of the case law. Each case depends upon its own facts . . ."

That case is perhaps very much at one end of the line and *Barr, Crombie & Co. v. Inland Revenue* (1945) (26 Tax Cas. 406), very much at the other. In the former the business of the taxpayer company was that of agents for manufacturers. At the relevant date they had far more agency contracts than the taxpayer here, however, and the sum under consideration by the Inner House was paid for cancellation of a contract which would have determined in any event in a relatively short time and in regard to which, as Lord Normand says, the taxpayer had no reasonable expectation of its further continuance.

However, junior counsel for the taxpayer points out that the present case is really distinguishable in a significant degree on its facts. First, the taxpayer here held but two agencies. Secondly, although the present agency was expressed to be determinable at relatively short notice, there would have been no reason to suppose that it would have been if all had gone well. And thirdly, as the commissioners pointed out, the effect of the loss of this contract, quoad the taxpayer's agency business was very substantially to depreciate his earnings: whereas in *Kelsall Parsons & Co. v. Inland Revenue,* the court pointed out that the taxpayer's earnings out of the agency business were not much different from what they had been before the cancellation of the material contract. I agree that this case differs in these respects from *Kelsall Parsons & Co. v. Inland Revenue.* But I am unable to agree that those differences are of such significance as to bring it from the territory, so to speak, of *Kelsall Parsons & Co. v. Inland Revenue* into that of *Barr, Crombie & Co. v. Inland Revenue.* On its facts, the present case more closely resembles *Inland Revenue v. Fleming & Co. (Machinery) Ltd.* (1951) (33 Tax Cas. 57), and, as already indicated, I must resist counsel's invitation to refuse to follow the Scottish line of authority.

To bring the case within the *Barr, Crombie* territory the taxpayer must be shown to have parted in truth and in substance, not merely with his rights and expectations under a contract *entered into in the ordinary course of his trade, but with one of his enduring capital assets, as it is called. On that sort of consideration this case might well have been different if the £4,000 had been paid because the taxpayer's goodwill had been damaged. In Barr, Crombie & Co. v. Inland Revenue the agency cancelled amounted to the substance of the whole business of the taxpaying company.* Its receipts accounted for nearly nine-tenths of the total earnings and its loss necessitated the complete reorganization of the company's business, a reduction in their staff, and the taking of new and smaller premises. In effect, a substantial part of the business undertaking had gone. Here, the taxpayer has been carrying on a business which for thirteen years has shown variations in the actual agreements which it has comprehended. The business has suffered something perhaps

of a disaster by reason of this quarrel with a valuable customer. But, beyond that, it seems to me it is not right to say that the taxpayer had his undertaking as a sales agent partially destroyed or taken away.

But, the matter being largely one of degree and so of fact, as Lord Normand said, I think the question is one of fact for the commissioners to find. On the facts of this case it seems to me that they were justified in finding, without any misdirection of law, that the amount awarded to the taxpayer was a taxable profit, i.e., a part of the profits or gains arising from the business for the year in question. Harman, J., said ([1955] 3 All E.R. at p. 551):

The taxpayer was a manufacturers' agent. He had other agencies from time to time and carried on business as an agent, and one of the incidents of such businesses is that one agency may be stopped and another begun. The fact that an agency was a key agency, and was therefore important to him and represented half of his income, seems to me to be irrelevant.

With the possible exception of substituting "inconclusive" for "irrelevant", I agree entirely with that statement; and I agree with what the judge said later (ibid.):

". . . it was a normal incident in this kind of business that an agency should come to an end, and it seems to me that the compensation paid is quite clearly income."

I agree with Harman, J., and I agree with him on the ground that this was a legitimate conclusion which the commissioners on the facts of the case were entitled to find. For these reasons, I think this appeal fails.

Earlier in the judgment Lord Evershed had referred to the taxpayers action for damages for breach of the agency contract and had said at page 757:

The taxpayer might have alleged that, apart from the loss of commission, the damage to him lay in the fact that, if the determination was wrongful, his goodwill as sales agent in this line of business was seriously impaired thereby. A reference to that matter is found in the commissioners' statement of facts. *I can well conceive that the taxpayer would have had a strong case for saying that damages would not be taxable, in so far as they were claimed because his goodwill as a sales agent had been impaired.*

and further on the same page:

I think one other inference must be drawn from the form of the judgment read in the light of the pleadings—I do not forget that this is a consent order under a settlement in which no doubt both parties considered all their alleged rights and defences. *On the face of it, it is impossible for the court to infer that this £4,000 or any part of it represented damages for the loss of the taxpayer's goodwill. I think the form of the pleadings and the amount of the damages really make that impossible.*

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Birkett, L.J. observed the same point at page 760 where he said:

> The taxpayer says through his counsel that it was a payment "for injury to the goodwill of my business". I agree with what the Master of the Rolls has said about that. The whole of this statement of claim, detailed as all the complaints are, contains no breath of a suggestion of that kind. It is confined wholly to the loss of commission. All the details in the pleadings, the defence and reply, really go to that purpose.

The question of whether the sum was paid for an injury to the goodwill of the business was thus resolved at the outset against the taxpayer but the issue still remained whether the sum was a profit of the trade and this issue was then decided on the facts of the case one of which was that the sum was not paid in respect of an injury to the goodwill of the taxpayer's business.

Of the cases cited that nearest in principle to the present one, in my opinion, is *Commissioners of Inland Revenue v. Fleming & Co. (Machinery) Ltd.*[1] where The Lord President (Cooper) said at page 61:

> The sum of £5,320 was paid to the Company as compensation for the loss of an agency which they and their predecessors had held for some 50 years as sole selling agents of explosives in Scotland for Imperial Chemical Industries, Ltd. and their predecessors. The problem thus belongs to a type exemplified by a number of recent cases in which, broadly speaking, the line has been drawn in the light of varying circumstances between, (*a*) the cancellation of a contract which affects the profit-making structure of the recipient of compensation and involves the loss by him of an enduring trading asset; and (*b*) the cancellation of a contract which does not affect the recipient's trading structure nor deprive him of any enduring trading asset, but leaves him free to devote his energies and organisation released by the cancellation of the contract to replacing the contract which has been lost by other like contracts. It is not possible briefly to formulate the distinction exhaustively or with complete accuracy, as the circumstances may vary infinitely; but a sufficient indication of the relevant considerations is found by contrasting such cases as *Van den Berghs, Ltd.*, [1935] A.C. 431, and *Barr, Crombie & Co.* [1945] S.C. 271, in which the payment was held to be of a capital nature with *Short Bros.*, 12 T.C. 955, and *Kelsall Parsons & Co.* [1938] S.C. 238, in which the payment was held to be of a revenue nature. These and other cases cited to us are relatively easy cases once the governing principle has been established for on their facts they all fall more or less unmistakeably on either the one side or the other side of the line. In this instance the difficulty is created by the fact that "the substance of the transaction" cannot easily be equated with the formal deed by which the transaction received effect. *Indeed I should almost be prepared to say that if attention is concentrated upon the business substance of this transaction the payment should be treated as a capital payment,* whereas if attention is concentrated upon the form the payment should be treated as a revenue payment.

[1] 33 T.C. 57.

In the *Fleming* case it appears from the reasons for judgment that the taxpayer lost on the question at issue largely because of the form of the transaction which provided for a payment as "compensation for the loss of the agency", which was the sum in question, and for a separate payment for which the taxpayer undertook to abstain from engaging in the explosives business and to do everything in its power to prevent any loss of goodwill or connection between the principal and its customers. It was conceded that the latter sum was not income.

Turning now to the facts of the present case I think the evidence makes it plain that the loss which the appellant faced when Doulton & Co. Limited made known its intention to terminate the agency was not merely one of the loss of one of a number of agencies but of an agency which accounted for a large proportion of the appellant's total business and in which was included a line of figurines which alone accounted for a considerable portion of the business and which was unique in the trade. For twenty years the appellant had had the agency for that particular line of goods and had built up the market for these figurines and for the other Doulton products which it sold. While the loss of the agency would set the appellant free to take on competitive lines a market for some other manufacturers' dinner ware would have to be promoted and built up and there was not even such an alternative with respect to the figurines for there was no comparable line on the market.

Against this background the appellant's letter of January 18th, 1954, using as it does expressions such as "take-over", arriving at a valuation . . . of an established earning power, which henceforth will accrue to you", "capitalized value" and "price" is clearly a request for payment for the loss of what the appellant regarded as its interest in the earning power and goodwill of the business in Doulton products on the Canadian market, a loss which the appellant expected to sustain as a result of the action which Doulton contemplated taking.

In this respect the case differs widely from the situation in *Wiseburgh v. Domville* where as pointed out in the passages quoted no claim in respect of damage to or loss of goodwill had been asserted and it is more nearly akin to the payment in the *Fleming* case for the undertaking not

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to carry on the explosives business and to assist in retaining goodwill. Moreover, while the settlement ultimately agreed upon in the present case differs in terms from that asked in the letter of January 18th, 1954, when one considers that the agency was said to produce $75,000 a year after taxes, for practical purpose the settlement agreed upon was the equivalent of the amount claimed. Nor is there in the changes of expression in the appellant's later letters, one of which refers to "loss of our valued agency" and another to "damages on termination of our contract", anything which in my view alters the substance of that for which a settlement was originally asked. In substance what appears to me to have happened was that in its letter of January 26th, 1954, the appellant altered its claim or price of $250,000 and offered in its place two alternatives, the first of which involved a continuation of the agency for roughly one year plus a payment of $175,000 in cash or preferred shares of the Doulton subsidiary and the other a continuation of the agency for almost two years plus a payment of $100,000 in cash or preferred shares of the subsidiary and it was the latter alternative which formed the basis of the settlement ultimately made. But neither this nor the letter which accompanied the payment, nor the reply to it in my view made any change in what the claim or price was for or in what the payment represented in the appellant's hands. Indeed the Doulton letter of January 2nd, 1956, which accompanied the payment, in referring to "your company's claim for damages for loss of rights ... on the cancellation of the agreement" appears to me to confirm that the settlement was a settlement of the claim which had been asserted.

One may, I think, usefully examine the payment from another angle as well. In my view it was clearly not a payment for arrears of earned commission or in lieu of earned commission for the appellant received the commissions earned to the end of 1955 and though the Doulton letter of April 29th, 1954 referred to commissions on goods ordered before but invoiced after December 31st, 1955 the business was so arranged that there were no commissions or practically none to which this provision could apply. To the extent that there were any such commissions, I think, the payment would represent taxable income. Nor was it a payment in lieu of commissions that might have been

earned to a normal termination of the agency contract and which were lost because of a premature termination of it. So far from there being a premature termination the effect of the arrangement was to defer termination far beyond the time when it might lawfully have been brought about. Nor is the sum a payment in lieu of notice or a payment made to obtain an early termination of the agency or a bonus for services rendered, for no claim for it was put forward by the appellant on any such basis and no such basis is suggested in the correspondence or in the other evidence. Nor is the payment merely one referable to an alteration of the terms of a contract made in the course of the appellant's business. Such an explanation in my opinion does not account satisfactorily for a payment of such size and particularly so where the alteration of the contract was at the appellant's request and to its advantage.

On the whole therefore having regard to the importance of the Doulton agency in the appellant's business, the length of time the relationship had subsisted, the extent to which the appellant's business was affected by its loss both in decreased sales and by reason of its inability to replace it with anything equivalent, to the fact that two of the appellant's employees became employees of the Doulton subsidiary on the termination of the relationship and the fact that from that time the appellant was in fact out of that part of its business, both as an agent and as a wholesale dealer, and particularly to the nature of the claim asserted in respect of which the payment was made, I am of the opinion that, except in so far as it was a consideration for services rendered to Doulton & Co. Limited, in connection with the take-over by its subsidiary, which is admitted to be income, and except in so far as it took the place of commissions on sales of goods ordered before, but invoiced after December 31, 1955, the payment in question was not income from the appellant's business, but was referable to the appellant's claim for loss of what it and Doulton Co. Limited as well considered to be the appellant's interest in the goodwill and business in Doulton products in Canada. In my view this was, to use Lord Evershed's expression, "a capital asset of an enduring nature". It was one which the appellant had built up over the years in which it had the Doulton agency and which

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on the termination of the agency the appellant was obliged to relinquish. The payment received in respect of its loss was accordingly a capital receipt.

The appeal will therefore be allowed with costs and the assessment referred back to the Minister to be revised in accordance with these reasons.

Judgment accordingly.

1961

Oct. 2, 3, 4, 5
Nov. 3

1962

Mar. 1

ONTARIO ADMIRALTY DISTRICT

BETWEEN:

AMERICAN EXPORT LINES INC. .....PLAINTIFF;

AND

PORT WELLER DRY-DOCK LIMITED ..DEFENDANT.

Shipping—Action for damage to ship occasioned by negligence in dry-docking—Undertaking by plaintiff to be responsible for damage to ship and cargo resulting from dry-docking with cargo on board or distribution of cargo does not exempt defendant from liability for loss suffered by negligent dry-docking.

The action is for damages done to the hull of plaintiff's ship the *Extavia* in a dry-dock operated by the defendant at the northerly end of the Welland Canal. Prior to the dry-docking the ship (loaded with a cargo of well over 2,000 tons) on a voyage from Milwaukee to Montreal grounded and it was to have ascertained any damage occasioned by this accident that the ship was taken to defendant's dry-dock. Defendant did not wish to deal with a loaded ship and after some negotiations plaintiff company sent defendant a telegram reading as follows: "We confirm telephone agreement Friday to assume responsibility for damage to vessel and cargo which may result from dry-docking with cargo on board or distribution of cargo".

In docking the ship was not docked squarely with the keel mid-way on the keel blocks which had been placed there to support it and in the result there was certain buckling along the underbody of the hull from about midship forward to the stem which eventually had to be repaired and it is for the cost of these repairs that the action is brought. The defendant contends that it was released from all liability for any damage by virtue of the telegram sent it by plaintiff's officer.

Held: That the damage to the ship was not caused by the presence of the cargo on board but was caused by the faulty docking and neglect to take precaution to sight adequately and carefully what the position of the ship was before it was lowered to the blocks.

2. That the defendant is not exempted from liability for the negligence found by the Court by virtue of the telegram since to have the exemption go that far it must be shown that the negligence complained of was a direct result from the presence of the cargo on board or from its peculiar distribution.

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ACTION to recover damages sustained by plaintiff's ship.

The action was heard before the Honourable Mr. Justice Wells, District Judge in Admiralty for the Ontario Admiralty District at Toronto.

F. O. Gerity, Q.C. and *R. Chaloner* for plaintiff.

J. L. G. Keogh, Q.C. for defendant.

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

WELLS D.J.A. now (March 1, 1962) delivered the following judgment:

This action arises out of damage done to the hull of the ship *Extavia* in a dry-dock operated by the defendant toward the northerly end of the Welland Canal. The dock is east of the Canal and is entered at its west end. It is a large dock some 750 feet in length and is situated slightly south of Lock No. 1 on the Lake Ontario side of the Canal not far from its entry at Port Weller.

It appears that previous to this dry-docking, on its way down the Welland Canal from Milwaukee to Montreal the vessel grounded and in efforts to get it off, the propellers were observed to strike some object in the water. It was to have any damage occasioned by this accident ascertained and if necessary, any bent propeller blades replaced, that the ship was taken into the defendant's dry-dock at Port Weller. In the course of its first docking the ship was not docked squarely with the keel mid-way on the keel blocks which had been placed there to support it and in the result there was certain buckling along the underbody of the hull from about midship forward to the stem which eventually had to be repaired and it is for the cost of these repairs that this action is brought.

At the time of these events the ship was loaded with a cargo weighing approximately some 2,987 tons. The defendant company had not dealt with a ship loaded with cargo and at first requested that the cargo be removed. This the

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plaintiff company was very loathe to do and finally, after some negotiations between the parties, an agreement was reached to dock the ship without removing the cargo. The arrangement reached between the parties is outlined in a telegram which was sent by an officer of the plaintiff company, Mr. R. F. Pitcher. It reads as follows:

> We confirm telephone agreement Friday to assume responsibility for damage to vessel and cargo which may result from dry-docking with cargo on board or distribution of cargo.

At the time he sent the telegram Mr. Pitcher was the Claims Manager of the plaintiff company. It is reasonably clear on the evidence that this docking was the first time the defendant company had docked an ocean-going vessel of the size and weight of the *Extavia*. It is true that they had dealt with certain smaller and lighter vessels using the old St. Lawrence Canal system. These vessels, however, had a much lesser draught and were much lighter ships than the *Extavia*. The dead weight of the *Extavia* appears to have been approximately the gross figure of 9,000 tons. The cargo had a weight of about one-third of this or 2,981 tons. The blocks provided by the defendants for the ship to rest on when the dry-dock was drained were a series of blocks down the centre on which the keel of the ship was to rest. There were two rows of blocks on either side of this centre line which have been described to me as skow and bilge blocks and it was the opinion of the defendant that if the ship were set squarely on these blocks they were sufficient to hold it upright and properly support it in the dry-dock when the dock had been drained of the water it contained.

The ship was brought to the dry-dock on May 25, 1959 and during the docking operation it was entirely under the direction and control of men employed by the defendant. Unfortunately, while it was brought in daylight, by the time the operation was completed it had become dark. When the ship finally settled on the blocks, representatives of the plaintiff and the defendant went down to inspect the hull with the aid of flashlights. A crackling sound was heard and on investigation it was discovered that the ship had settled on the blocks off centre to port of the centre line. This, of course, led to a complete maldistribution of weight and the blocks which were of fir wood, were compressed and in some cases split. While at the stern of the ship the ship was only two inches off

centre, at the bow it was between two feet and two feet two inches off the centre line. What happened was a serious denting of the plates on the port side, the dents in some cases being as deep as two inches from the normal surface of the plate. There was apparently very little damage on the starboard side and the bulk of the damage occurred to the B strake plating on the port side. The worst damage was between the bow and a point aft about mid-way. There was some small damage on the starboard and some damage to the keel plating.

Two surveyors examined the ship on behalf of the owners. One of these represented the American underwriters and the other represented the British underwriters. A number of plates in the area of the B strake plating were found to be heavily buckled and it is interesting to note that in Mr. Warkman's report he noted that these indentations clearly bore the marks of the keel blocks. In summing up his findings he said this in the report:

> The damages were readily discernible as they bore the definite imprint of the dry-docking blocks inway the indentations. The vessel was docked off centre to port side, the forward keel plating being practically off of the keel blocks, consequently transferring the weight to the Port side where the B Strake plating was found to have sustained the most damages as it was carrying the additional weight.

After the first docking when the ship was first examined, after the dock had been substantially drained, by the two surveyors I have mentioned and Mr. Fenton who was the representative of the owners, they heard what was described as a continuous granulating or crushing sound and equipped with flashlights they went forward to try and ascertain what was the cause of this. As I have already said they found the ship docked off centre and they apparently were both of the opinion that there was a serious danger that she might roll over onto her port side. Accordingly, Mr. Fenton as representative of the owners, asked that the vessel be refloated and taken out to permit the replacing of the damaged blocks and a subsequent redocking. This was done and the second time the vessel was placed squarely on the keel blocks and despite the weight of the cargo and of the ship itself, no further damage or buckling occurred. It is, I think, a fair inference that the damage which occurred at the time of the first docking obviously occurred from the uneven support which the keel blocks offered when the ship was not centred on them properly.

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The blocks themselves were some four feet in width and apparently were quite equal to support the keel of the ship if it was placed squarely along their midline. This unfortunately, was not done and when the blocks because of the uneven distribution of weight, were crushed and gave way, in some instances the maldistribution of weight was very much aggravated.

I am not able to find in the evidence any evidence as to whether this was caused by the weight of the cargo or not. It is, I think, significant that no further damage of any sort occurred when the second docking took place and when the ship was fairly lined up along the midline. There was evidence that the machinery and boilers and motors of the ship were placed about midship and that even without cargo there was a very substantial weight. In this respect reference may be made to the evidence of the surveyor Rozycki and it may very well be that the maldistribution of support which resulted from the faulty docking, would have caused the damage even if the cargo had been removed beforehand as there was still a very considerable weight in the ship quite apart from its cargo. For some reason none of the surveyors were asked about this save Rozycki who thought the dents might be deeper because of the cargo. The defendant's surveyor was not called at all. The two surveyors who did testify, however, are perfectly clear as I have already noted, that none of the indentations which appeared, did so after the second docking.

As there is a complete denial of any liability for negligence by the defendant, it will be convenient to first discuss the facts and then to deal with the various defences in law which the defendant raises.

I have already described the situation of the dry-dock and as I have noted, it is entered on the west and is about 750 feet long. The *Extavia* at its greatest length from hull to the overhang of its stern is some 420 feet long. She was brought into the dry-dock under the control of the defendant's employees. Mr. Cleet who was substantially in charge of the operation, testified that her stern was about 50 feet from the dock gates which give on to the Welland Canal. For purposes of strength they project outwards and I am not sure whether the extra space given by this is taken into account in the figure of 750 for the length of the dock

or not. But it is quite clear, I think, that when the ship was brought in to be lowered on the blocks there was something like about 300 feet from the stem of the ship to the east wall of the dry-dock. It may be a little more or a little less than that but the figure 300 appears from the evidence to be a convenient approximation. There were erected on the east wall of the dry-dock two angle iron sights standing about four feet high to line up the centre line of a ship with the centre line of the keel blocks. Three hundred feet or even two hundred and eighty feet is a very considerable distance when one is sighting to ascertain the centre line of a ship as long as the *Extavia* and the device which was admittedly used on the second docking was that of putting up wooden battens on the centre line of the keel blocks between the angle iron sights on the east wall and the stem of the ship. This additional aid was not, in my opinion, used on the first docking. The failure to use these sights in my opinion, probably accounts for the docking off centre which I have described. The evidence is not at one on this point.

McIlravey who was the deputy foreman at Port Weller, swore that two such battens were erected on the first occasion; that one was about 50 feet east of the bow of the *Extavia* when she came to rest and the other one was about 50 feet further on. I can only say that from my observation of him in giving his evidence and considering this statement along with that of the two surveyors who were called on behalf of the plaintiff, I am not able to believe him. Both Rozycki and Warkman who were the surveyors I have mentioned, said that when they examined the ship and discovered the situation in which she was lying, they did it by flashlight. It was admittedly after nine o'clock and it had become dark. They specifically looked for sighting battens as they called them, and found none. Mr. Warkman stated that he had suggested to Mr. Cleet that such battens should be put in for the redocking and they were so placed but there were none there the first time and they apparently went up forward of the ship and looked between the dock area of the ship and the east wall to make sure. Rozycki confirms this, Fenton confirms it, and I must find as a fact that there were no battens used on the first docking.

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What caused the vessel to go to port of the centre line of the blocks? An examination of the measurements of the ship in the docking plan which was given to the defendant indicates that the *Extavia* had very fine lines and it is quite obvious from the exhibits which were filed by way of photographs, that she had a fine flaring bow. The dry-dock into which she was brought was a wide one and was capable of holding two ships abreast. Consequently when the ship was brought into the dock she was controlled by lines which ran to the north wall of the dry-dock and one large one a considerable distance over to the south wall. It was only the north wall to which the ship was at all near and the distance between the north wall and ship was controlled by two shores eight inches square fir timbers which were kept floating to the side of the vessel and which were controlled by men holding lines on the north wall and on the ship. There was one of these pieces of timber aft and one forward of the midship section but apart from this it is impossible to say just where they were. Apparently, the proper length for them had been calculated from the docking plan by checking the sections of the ship which were shown there against the distance from the centre of the keel blocks to the north wall and deducting the space which the ship actually occupied.

It is to be observed that this docking procedure was entirely in the hands of and under the control of the defendant's servants and workmen. Once the ship was in, the only lines on the ship at the forward end were lines from the bow to the north wall. Apparently the distance to the south wall was too great. It is quite obvious that while all these aids to placing the ship were there, that the real guidance must have come from the man on the sights at the east wall and without any interim sighting battens it is to me rather obvious that the possibility of error at a distance of 280 or 300 feet was considerable. If there had been interim sights, checking on the accuracy of the sights at the east wall would have greatly improved as it undoubtedly was on the occasion of the second docking. In this connection it is interesting to look at Ex. 20 which shows a sister ship of the *Extavia* in the same dock at a later time in the same year.

At 300 feet an error of two feet two inches is not a very large one but in this case it proved a very damaging error and while by reason of the arrangement between the plaintiff and the defendant the plaintiff had assumed responsibility for damage to the vessel and cargo which might result from dry-docking with cargo on board or distribution of cargo, as I will presently demonstrate, I do not think that was a complete protection for the defendant and it did not remove from the defendant some responsibility to bring the *Extavia* down on the blocks at the proper place. My impression from the defendant's witnesses was that it assumed that it was entirely protected by the telegram and in consequence did not take too many precautions for exactness. Both Cleet and McIlravey, who were between them in charge of the operation, had very little co-ordination between them. It is significant, I think, that McGrath who in the end was at the stern end of the ship and Cleet, who was generally superintending the whole operation in a somewhat detached manner at the pumphouse where the valves of the dry-dock were controlled, could not see whether any sighting battens were used or not. One would have thought that Cleet, on whom the ultimate responsibility must rest, would not have left it in the rather careless way he did to his subordinates without checking all the details himself. This in my opinion, he did not do. There was the more reason that he should take this extra care when this was the first time a vessel of its size, weight and type had been docked in the dry-dock. It is true, that before he opened the valves he shouted to McIlravey and McGrath who both assured him all was well. But he did no personal checking himself.

In my opinion the defendant was negligent in docking the ship off centre and this was caused in my view by a failure to take proper precautions to see that the ship was properly centred on the keel blocks before the water in the dock was lowered and this happened largely because there were no interim sights between the sights on the east wall and the stem of the ship and because no very great care was taken to check even with what they had. It should have been apparent to the defendant that at the distance the bow of the ship was from the sight on the east wall, there was a very real possibility of error and faulty docking. My impression of all three men employed in

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supervising the docking was that they were not in the least worried by any of these matters. If my recollection is correct, Mr. Cleet or one of the men under him, expressed the opinion when it was discovered that the ship was off the blocks as it was, that they had done a pretty good job anyway.

The defendant takes the position that even if there was negligence on its part, it is effectively released by the terms of the telegram which was sent by the plaintiff to the defendant prior to the docking of the vessel. In that telegram as I have pointed out, the plaintiff "assumes responsibility for damage to vessel and cargo which may result from dry-docking with cargo on board or distribution of cargo."

Counsel are apparently in agreement on one thing and that is that the defendant in this case was a bailee of the ship for hire or reward. The duty of a bailee in such circumstances is succinctly set out in Halsbury's *Laws of England,* Third Ed., Vol. 2, p. 114, para. 225 in the article on Bailment as follows:

> 225. CARE AND DILIGENCE. A custodian for reward Amongst such custodians are included agisters of cattle, warehousemen, forwarding merchants, and wharfingers (story on Bailments (9th Edn.), s. 442). See also the following cases: *Scarborough v. Cosgrove,* (1905) 2 K.B. 805, C.A.; *Paterson v. Norris* (1914), 30 T.L.R. 393 (boarding-house keepers); *Olley v. Marlborough Court, Ltd.,* (1949) 1 K.B. 532, C.A.; (1949) 1 All E.R. 127 (proprietor of hotel which is not an inn); *Martin v. London County Council,* (1947) K.B. 628; (1947) 1 All E.R. 783 (managers of hospital). As to dock and harbour authorities, see title Shipping, is bound to use due care and diligence in keeping and preserving the article entrusted to him on behalf of the bailor. The standard of care and diligence imposed on him is higher than that required of a gratuitous depositary, and must be that care and diligence which a careful and vigilant man would exercise in the custody of his own chattels of a similar description and character in similar circumstances. HOLT, C.J., in *Coggs v. Bernard* (1703), 2 Ld. Raym. 909, at p. 916, says that the bailee must use "the utmost care", but this probably means *"talis qualem diligentissimus paterfamilias suis rebus adhibet",* and not the care required of the borrower of a chattel loaned gratuitously. See Jones on Bailments (4th Edn.), 86, 87; *Dean v. Keate* (1811), 3 Camp. 4; and see the note to that case, *ibid.,* p. 5.

In *Brice and Sons v. Christiani and Nielsen*[1], Rowlatt J. observed at p. 336: that the ordinary rule of law was that if a person who handled the property of another and handed it back in a damaged condition was liable unless he could say that the damage had not been caused by negligence on his

[1] (1928) 44 T.L.R. 335.

part, the same principle in my estimation would apply where the article is taken in to have work done on it for which the bailee is to be paid. Relying on this principle, counsel for the defendant asks that the only responsibility on the defendant was to use reasonable care and to make sure that its equipment was reasonably safe. I quite agree with his contention that the bailee is not an insurer as is a common carrier and I also agree that the defendant's responsibility for such a dry-docking was not to be negligent in such a dry-docking. At that point it is argued that the telegram is in effect a waiver for any negligence which may result from the dry-docking with the cargo on board and I have been cited a series of cases in which, under somewhat similar circumstances, the defendants had been relieved of responsibility. One of the most helpful of these is the decision of Karminski J. in the case of *The Ballyalton. Owners of Steamship Ballyalton v. Preston Corporation*[1]. This concerned what was known as Horrocksford wharf at the Port of Preston. The ship *Ballyalton* being loaded with a cargo of stone was on April 16, 1956, berthed at Horrocksford wharf and suffered damage owing to the unevenness of the bottom of the berth. The damage was found to be due to the defendant's negligence in supervising the berths at the wharf. A notice set out the conditions for use of the dock. It was provided by this notice that there was no insurance that the berths would always be level and that rates be charged and taken by the corporation therefor, vessels going to or using the same respectively and their cargo, must be and were at the risk of the owners or charterers and the burden of satisfying themselves that it was safe to use the quays and docks was placed on the ships making use of them.

The learned trial Judge held that the words of exemption in the notice were, on their true construction wide and unambiguous enough to cover negligence. He also held that apart from the exemption the liability of the defendants rested solely in negligence. In reaching these conclusions

[1] (1961) 1 All E.R. 459.

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he relied as to method of approach on the well-known passage in the judgment of Scrutton L.J. in the case of *Rutter v. Palmer*[1], and at p. 463 he said:

> My first task is to consider the general principles of construction of an exemption clause, and these are to be found in the well-known passage of Scrutton, L.J.'s judgment in *Rutter v. Palmer* (supra)
>
> > In construing an exemption clause certain general rules may be applied, the first of which is that the defendant ought not to be relieved from liability for the negligence of his servants unless clear and unambiguous words to that effect are used. In the second place the liability of the defendant has to be ascertained quite apart from the exempting words in the contract. Then, again, the particular clause in the contract has to be construed and considered, and if the only liability of the party pleading the exemption is a liability for negligence, the clause will more readily operate to discharge him: see *Reynolds v. Boston Deep Sea Fishing & Ice Co., Ltd.* (1922), 38 T.L.R. 429.

Rutter v. Palmer (1922) All E.R. Rep. 367; (1922) 2 K.B. 87 was a case where the owner of a motor car deposited the car for sale with a garage keeper on terms set out in a printed document, and the car was damaged by reason of the negligence of a driver employed by the garage keeper. The principles set out by Scrutton L.J., have been applied in cases where locks or berths have not been maintained in a safe state by their owners. Cf. *Forbes, Abbott & Lennard, Ltd. v. Great Western Ry. Co.* (1928), 138 L.T. 286; 17 Asp. M.L.C. 347, and *Jessmore (Owners) v. Manchester Ship Canal Co.* (1951) 2 Lloyds' Rep. 512.

I propose to subject the facts of the present case to the tests laid down by Scrutton L.J., bearing in mind particularly the words used by the defendants in their notice. Counsel for the plaintiffs rightly insisted that in construing exemption clauses the court should interpret them against the party putting them forward, unless satisfied as to their meaning. On the other hand, in seeking to arrive at a meaning, I have equally no doubt that I must look at the notice as a whole. It is easy to criticise the notice and to say that it could have been more clearly, and also more concisely, drafted. It might, for example, have been better in para. 3 to have said that vessels using the berths were at the sole risk of the owners or charterers. Cf. the terms of the Manchester Ship Canal Notice in *Jessmore (Owners) v. Manchester Ship Canal Co.* (1951) 2 Lloyd's Rep. at p. 525. But I have here to look also at the other terms used in this notice:

> . . . vessels going to or using the same . . . must be and are at the risk of the owners, or charterers, captains, or others interested in vessels or their cargoes and not of the corporation, who will not be responsible for and will repudiate any liability in respect of any damage either to vessel or cargo . . . the corporation will not be responsible for and will repudiate any liability in respect of any damage either to vessel or cargo resulting from using the quays or river diversion, or either of them, or taking the ground thereat or therein.

[1] (1922) All E.R. at 370.

I have considered *White v. John Warrick & Co., Ltd.* (1953) 2 All E.R. 1021, where a different exemption clause was held to exempt defendants from their liability in contract but not from negligence. But looking at this notice as a whole I have come to the conclusion that the words here used are adequate to exempt the defendants from liability for the negligence of their servants.

Adopting the mode of procedure indicated by Scrutton L.J. which has also been adopted and used by the Court of Appeal of Ontario in the case of *Porter & Sons v. Muir Bros. Dry-docking Company Limited*[1], per Grant J.A. at p. 460, I have already come to the conclusion that the defendant was negligent in not taking more precaution in docking the vessel for the first time and coming now to the words of the telegram, I may say that I have been referred to many cases. One of these was the case of *Pyman Steamship Company v. Hull and Barnsley Railway Company*[2]. There the words, in my opinion, are much wider than the telegram in the present case. They provide that the owner of a vessel using the graving dock must do so at his own risk, it hereby being expressly provided that the company are not to be responsible for any accident or damage to a vessel . . . whilst in the graving dock, whatever may be the nature of such accident or damage or howsoever arising. The Court of Appeal properly held on this language that it must be read to cover failure to perform any obligation arising from the contract and as covering negligence arising from want of care in the performance of such obligation.

In the case of *Reynolds v. Boston Deep Sea Fishing and Ice Company, Limited*[3], which was a decision of Greer J., the exemption clause provided that:

> All persons using the slipway must do so at their own risk and no liability whatever shall attach to the company for any accident or damage done to or by any vessel either in taking her to the slip or when on it or when launching from it.

It was held that while this clause did not expressly mention negligence, it was wide enough to protect the defendants for liability for such negligence.

In the case of *Forbes, Abbott and Lennard, Limited v. Great Western Railway Company*[4], the clause provided that "all barges and vessels while in Chelsea Dock are at the sole

[1] 63 O.L.R. 437.
[2] (1915) 2 K.B. 729.
[3] (1921) 38 L.T.R. 22.
[4] (1927) 44 T.L.R. 97.

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risk of owners or persons bringing or causing the same to be brought into the dock." These words were held sufficient to exempt the defendants from liability for negligence.

I am urged to take the view that the words in the telegram to the effect that the plaintiff assumes responsibility for damages to vessel and cargo which may result from dry-docking with cargo on board or distribution of cargo are wide enough to exempt the defendant from liability for the negligence I have found. In my opinion the exemption does not go that far. Before it operates I think it must be shown that the negligence complained of was a direct result from the presence of the cargo on board or from its peculiar distribution.

In the view I take of the matter the damage was not caused by the presence of the cargo on board. It appears to have been assumed that the additional weight would have caused the damage but I am not conscious of anything in the evidence which narrows it down to this one cause and the fact that such damage did not occur at the time of the second docking when the ship was properly placed on the blocks is a strong factor, in my opinion in supporting the view I have taken that the damage caused was not caused by the presence of the cargo on board but was caused by the faulty docking and the neglect to take precaution to sight adequately and carefully what the position of the ship was before it was lowered to the blocks. It may be that if it can be shown that the main and proximate cause was the cargo, that the defendant should be entitled to whole or partial relief but in my view of the evidence this has not been demonstrated and the direct and proximate cause of the accident was not the additional weight of the cargo but the faulty docking. It may very well be that under certain circumstances the defendant may be excused for negligence but on the facts of the case as I see them and as it has been proved before me, in my view, the exemption clause does not come into operation and is not wide enough to cover the circumstances which I think were the direct and proximate cause of the injury to the ship.

Under these circumstances there will be judgment for the plaintiff. The precise amount of the damages were not proved before me. In point of fact the *Extavia* was not repaired until nearly a year later during which time it

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suffered other accidents which also damaged the hull and while the gross amount of the repairs is known, the amount of the damages suffered by the dry-docking in the defendant's dock have not been determined. To do this, on the consent of the parties and the consent of the Surrogate Judge, there will be a reference to the Surrogate Judge of the Admiralty Court in this District to ascertain the true amount of the damages. If Mr. Rozycki's opinion is correct, the depth of the dents may have been increased by the presence of the cargo. If the Surrogate Judge is satisfied with this some allowance may be made to the defendant for the increased severity of the damage. On the determination of such it may be necessary for the Surrogate Judge to have assessors. I prefer to leave that question to his discretion and it will be for him to decide whether they are necessary or not. The plaintiff should, of course, have his costs of the action to date and the costs of the subsequent reference to the Surrogate Judge I leave in the discretion of the Surrogate Judge.

Judgment accordingly.

BETWEEN:

1961

C. H. BOEHRINGER SOHN .....PLAINTIFF;

Oct. 30, 31, Nov. 1, 2, 3, 6, 7, 8, 9, 10, 15, 16, 17, 21, 22, 23, 27, 28, 29, 30, Dec. 1, 4, 5, 6, 7, 8, 11, 12, 13, 14, 15, 18, 19, 20

AND

BELL-CRAIG LIMITED .....DEFENDANT.

1962

Mar. 21

Patents—Infringement—Claims for substances prepared or produced by chemical process and intended for food or medicine—Substance claim must be limited to that substance when produced by process for its preparation claimed and particularly described or an obvious chemical equivalent—To validate product claim process claim must be valid—The Patent Act, R.S.C. 1952, c. 203, ss. 2(d), 28(1), 35, 36, 41(1) and (2).

The plaintiff sued for infringement of its patent for an invention entitled "process for the production of substituted morpholines" alleging that the defendant by selling phenmetrazine hydrochloride tablets had infringed claim 8 of the patent, a claim for "2-phenyl-3-methylmorpholine when prepared by the process of claim 1, 2 or 3 or an obvious chemical equivalent". (Phenmetrazine is the generic name for 2-phenyl-3-methylmorpholine.) The defendant admitted the sale but denied infringement and attacked the validity of claims 1, 2, 3, and 8.

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The specification describes in general terms certain processes for the production of a class of substituted morpholines large enough to include many billions of them but nowhere until claim 8 refers to 2-phenyl-3-methylmorpholine except by way of an example of the class. The defendant contended that the specification should be construed as disclosing but a single invention of processes for making the whole class of substances claimed and on the basis of this construction raised a number of objections to the patent. The plaintiff submitted that as a matter of construction the specification disclosed two inventions, one relating to the class of substituted morpholines, the other to the single substance 2-phenyl-3-methylmorpholine.

Held: That to give meaning to the specification as a whole it must be read as disclosing two inventions, one relating to the class of substituted morpholines and the other relating to the single substance 2-phenyl-3-methylmorpholine included in claim 8.

2. That as claim 1 is a claim for a process for the making of the whole class of substances referred to in the specification and does not state the starting material from which 2-phenyl-3-methylmorpholine may be made, it does not state the essential feature of a process for making 2-phenyl-3-methylmorpholine, and it cannot be regarded as a claim of the kind required by s. 41(1) of the *Patent Act* as interpreted in the *Winthrop case*. The substance claim of claim 8 therefore is not limited, as it should be to comply with s. 41(1), to that substance when produced by a process for its preparation which is claimed and claim 8 is accordingly contrary to s. 41(1).

3. That under s. 41(1) of the *Patent Act* a claim for a new substance to which the subsection applies must be limited not only to that substance when prepared by methods or processes which have been claimed but also to that substance when prepared by the methods or processes which have been particularly described or their obvious chemical equivalents, and since the claim to 2-phenyl-3-methylmorpholine in claim 8 is not limited to that substance when prepared by the methods or processes which are particularly described or their obvious chemical equivalents. Claim 8 is broader than s. 41(1) permits and is accordingly invalid.

4. That in a patent to which s. 41(1) of the *Patent Act* applies, the process claim which must accompany a product claim for a new substance must itself be a valid claim. A claim to an exclusive property to which the inventor is not entitled and which is therefore not authorized by the statute will not serve the purpose.

5. That a claim for processes which produce products which are not useful in the patent sense lacks utility and is therefore invalid. On the evidence it is improbable that all or the majority or even a substantial number of the conceivable substances comprised within the class defined in claim 1 have the utility referred to in the specification, claim 1 is accordingly invalid and because it is invalid, claim 8 is invalid as well.

6. That for the purpose of obtaining the pharmacological results obtained by oral administration, phenmetrazine hydrochloride is an equivalent of phenmetrazine and if made by one of the processes mentioned in claim 8, its sale would constitute an infringement of claim 8.

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7. That on the facts the process by which the allegedly offending material was made did not involve as one of its steps the process of claim 1 as applied to the production of 2-phenyl-3-methylmorpholine from a particular diethanolamine of the class but did involve a process which was an equivalent of the process of that claim when applied to the production of 2-phenyl-3-methylmorpholine from that diethanolamine. It was not however an obvious chemical equivalent of the process of claim 1 within the meaning of s. 41(1) of the *Patent Act* and the claim of infringement accordingly fails.

Re May & Baker Ltd. et al. 65 R.P.C. 255; 66 R.P.C. 8; 67 R.P.C. 23; *Winthrop Chemical Co. Inc. v. Commissioner of Patents* [1948] S.C.R. 46; *Commissioner of Patents v. Ciba* [1959] S.C.R. 378 at 383; *McPhar Engineering Co. of Canada Ltd. v. Sharp Instruments Ltd.* 21 Fox P.C. 1 at 55, referred to.

ACTION for infringement of patent.

The action was tried before the Honourable Mr. Justice Thurlow at Ottawa.

Christopher Robinson, Q.C. and *R. S. Smart* for plaintiff.

I. Goldsmith and *R. S. Caswell* for defendant.

THURLOW J. now (March 21, 1962) delivered the following judgment:

In this action, the plaintiff claims an injunction and other relief in respect of alleged infringement by the defendant of claim 8 of Canadian patent No. 543559, which was granted to the plaintiff on July 15, 1957. The invention referred to in the patent is entitled "Process for the production of Substituted Morpholines" and claim 8 is a claim for "2-phenyl-3-methylmorpholine, when prepared by the process of claim 1, 2 or 3 or an obvious chemical equivalent".

The plaintiff's complaint is that the defendant has infringed claim 8 of the patent by selling in Canada phenmetrazine hydrochloride tablets. Phenmetrazine is a trivial or generic name for 2-phenyl-3-methylmorpholine. The defence, while admitting that the defendant sold tablets designated as phenmetrazine hydrochloride—which the evidence shows they were—denies infringement and also raises a number of objections to the validity of claims 1, 2, 3 and 8.

The importance of phenmetrazine lies in its usefulness for certain pharmacological purposes. The particular pharmacological field is that involving the use of substances known as sympathomimetic amines which have effects resembling in some one or more ways the effects of adrenalin. These substances generally are classed as stimulants.

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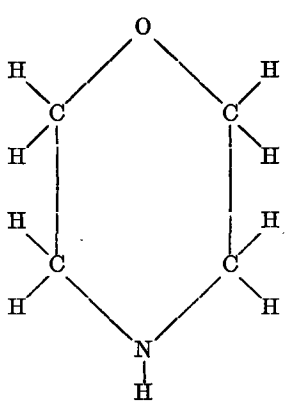
One of the best known substances of this class is amphetamine or benzedrine, the principal effects of which are to produce stimulation and defer tiring, to depress the appetite, and to increase the blood pressure and pulse rate. For a considerable time it was thought that it would be impossible to find a stimulant without having these three effects more or less associated, but eventually it was discovered that other substances resembling amphetamine in chemical structure could be made which would retain selectively the stimulating effect without exhibiting too much cardiovascular effect or anti-appetite effect and the reverse was also true. In general, it was desirable to have drugs which as far as possible would produce one effect without the others. Thus in the treatment of obesity, for example, it frequently happens that the patient has high blood pressure and it is therefore desirable to make use of a substance which, while deferring tiring and depressing the appetite, will not further raise the blood pressure. It has also been discovered that while all of these substances operate through the brain rather than upon the muscles, the type of stimulation produced by such substances may vary with the substance used, the effect in some cases being to stimulate mental activity more than or rather than locomotor activity. At the time of the invention of the patent in suit, at least four such substances, viz. benzedrine, norephedrine, pervitine and ephedrine, each having the three effects in similar though varying degrees, were known and in use but it is admitted that phenmetrazine was not known or used by anyone before that date. Phenmetrazine, according to the patent specification, is superior to benzedrine (pervitine) "inasmuch as it causes the particularly desired effect of deferring the tiring whilst being less poisonous and less stimulating". It can, however, be used in larger doses to "produce stimulation which however will not be accompanied by a corresponding increase in blood pressure". While the evidence does not make plain just how far these assertions of the specification are supportable in fact, the evidence of Dr. Belleau as to the use to which this substance is put, coupled with the evidence of commercial production and sale of it and the prolonged efforts which Industria Chimica Profarmaco, S.p.A., the Italian company which manufactured the allegedly infringing material, put

forth to find a way to make it satisfies me that phenmetrazine in fact has advantages for some purposes over the four previously known drugs having similar effects, and that the discovery of its activity represented an advance on what had previously been known.

Before turning to the specification, I shall endeavour to explain in the hope of making what follows more intelligible what I think the evidence indicates as to certain chemical terms and concepts pertaining to substituted morpholines and the diethanolamines from which they are prepared.

Morpholine is a single substance having in its molecular structure four atoms of carbon, one atom of oxygen, one atom of nitrogen, and nine atoms of hydrogen. Each carbon atom has four bonds or valencies by which it may be linked to other atoms in the molecule of a substance. The oxygen atom has two such valencies, the nitrogen atom three, and each hydrogen atom one. In the morpholine molecule, the carbon, oxygen and nitrogen atoms are arranged in a hexagonal ring formation with the oxygen and nitrogen atoms at opposite corners of the hexagon. Two of the hydrogen atoms are linked to each of the carbon atoms, and the remaining hydrogen atom is linked to the nitrogen atom. The structural formula of the molecule so formed may be represented as follows:



This is the single substance, morpholine. Substances are known, however, wherein the position of one or more of the hydrogen atoms linked to carbon atoms in this structure may be occupied by some other atom or group of

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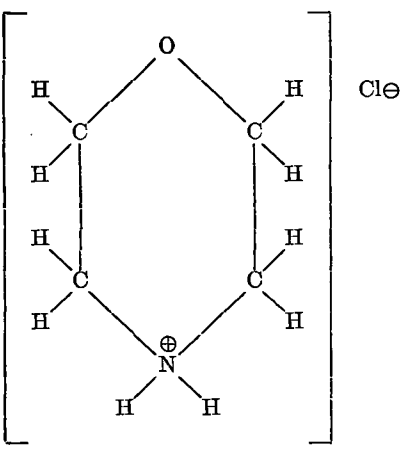
atoms. Such substances are referred to as substituted morpholines, the common characteristic being the singly-bonded hexagonal ring structure composed of four carbon atoms, one oxygen atom, and one nitrogen atom, with the latter two opposite to each other or separated from each other by two carbon atoms on either side.

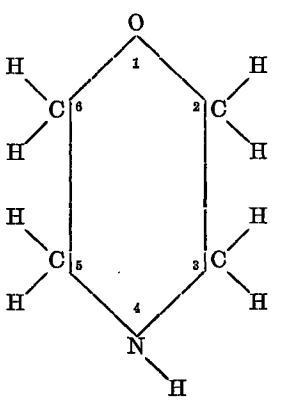
Morpholine is a base and, when put in an acid, it reacts to form a salt. Using the hydrochloride as an example, the structural formula of such a salt may be represented thus:



In this representation it will be observed that, in addition to the single hydrogen and two carbon atoms, which are linked to the nitrogen atom in the morpholine base, the nitrogen atom also carries or has linked to it an additional hydrogen proton which is considered to be a hydrogen atom without the negative electron which normally forms part of such an atom. The negative electron is shown in association with the chlorine atom which is represented as associated with the ring structure as a whole. This, however, is only a way of portraying the molecular structure and no matter how it may be portrayed the morpholine hydrochloride molecule differs from the morpholine molecule in that it includes in addition to the atomic components of morpholine an additional atom of hydrogen and an atom of chlorine. As there are several thousand known acids there can be several thousand different salts of morpholine. The same applies to each substituted morpholine. It may not be amiss to mention as well at this stage that

hydrochloric acid is normally present in the stomach fluid of human beings and because this acid may be expected to react immediately with a morpholine—whether substituted or unsubstituted—to form the hydrochloride salt of the morpholine, the result of taking a small quantity of the morpholine into the stomach can be expected to be precisely the same as if the hydrochloride salt of the morpholine were taken instead. It does not, however, follow that the result would be the same if any other salt of the morpholine were taken.

For reference purposes, the corners of the characteristic morpholine ring are numbered from 1 to 6, that occupied by the oxygen atom being numbered 1 (thus



)

and the numbers 2, 3, 5 and 6 appearing in the name of a substituted morpholine refer to the positions on the ring of substituents occupying the positions of hydrogen atoms linked to the corresponding carbon atoms in morpholine. Accordingly, a substance having, for example, a phenyl (C_6H_5) group linked to a carbon atom in number 2 position in place of one of its hydrogen atoms would be known as 2-phenyl morpholine, and if the molecule also had a methyl ($C H_3$) group linked to the carbon atom in number 3 position instead of one of its hydrogen atoms the substance would be known as 2-phenyl 3-methylmorpholine. Examples could be multiplied indefinitely, using other substituents and the other positions.

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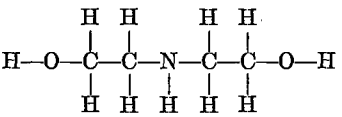
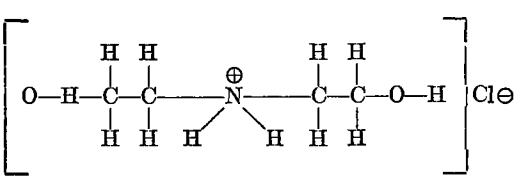
I turn now to the substance known as diethanolamine, which, like morpholine, is also a single substance. Its empirical formula is $C_4H_{11}O_2N$, and its structural formula may be shown thus



While the structure is shown in line or as a chain, the molecule is considered to be U-shaped, the nitrogen atom being at the base of the U. It will readily be perceived that, if this structure were to release two atoms of hydrogen and one of oxygen from the hydroxyl (OH) groups at the two ends, the remaining oxygen atom and the carbon atom on the opposite end would each have one bonding position available for the formation of a linkage between them, and that if such a linkage were formed the resulting substance would be morpholine.

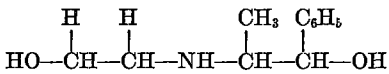
Diethanolamine, too, is a base which, when put into an acid, will react to form a salt which, using the hydrochloride as an example, may be represented thus:



The salts of diethanolamine are of course different substances from diethanolamine itself. As in the case of morpholines, there may also be substances in which the position of a hydrogen atom attached to a carbon atom in diethanolamine is occupied by some other atom or group of atoms. Such substances are known as substituted diethanolamines.

For reference purposes, the carbon atoms on one side of the nitrogen atom are referred to as α and B, the α carbon atom being that linked directly to the nitrogen atom, and those on the other side of the nitrogen as α^1 and B^1, α^1 being the one linked directly to the nitrogen atom.

It is admitted by the parties that ring closure of diethanolamine to form morpholine has been known since at least 1889 and that, before the date of the invention of the patent in suit, the formation of morpholines generally by ring closure of the corresponding diethanolamines was common knowledge in the art. It is also admitted that the diethanolamine of the formula



known as B-phenyl - α - methyl - B,B1 - dihydroxy-diethylamine which if ring closed would give 2-phenyl-3-methyl morpholine, has been known since at least 1929. The following further facts pertaining to prior knowledge are stated in the specification.

> Processes for the production of morpholine derivatives are already known, whereby diethanolamines were treated e.g. by heating to temperatures to 160-180°C with 70% sulphuric acid, in order to acquire the morpholine ring closure.
>
> However, it is particularly necessary when producing substituted morpholines, to find specially mild reaction conditions for the ring closure. In this case there exists namely, the danger of undesired side reactions, which can be brought about by the influence of the temperature or the acids employed for the ring closure.
>
> In U.S. Patent Letters 2,566,097 a process is described according to which when the substituted diethanolamine is allowed to stand in solution, ring closure already takes place. However, such an easy ring closure is only limited to very definite individual cases, whereas generally vigorous conditions are necessary.

It was also common knowledge to a chemist that a diethanolamine, on being put into an acid, would not remain a base but would react at once with the acid to form a salt, and that the ring closure would take place thereafter. By the same token it was also known that, on treating a diethanolamine with an acid to obtain the ring closure, what is produced in the reaction is the morpholine salt of the acid used and that, in order to obtain the morpholine, a further process of treating the salt with an alkaline substance such as sodium hydroxide or ammonium hydroxide would be required.

I turn now to the specification. This, it may be noted, does not purport to relate to the invention of 2-phenyl-3-methyl morpholine alone. On the contrary, it describes in general terms certain processes for the production of a

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class of substituted morpholines large enough to include many billions of them most of which have never been made or tested by anyone, and nowhere in it until one reaches claim 8 is there any reference to 2-phenyl-3-methyl morpholine except as an example cited to describe advantages which all members of this very large class of substances or possible substances are claimed to have and except in two of the examples of how the processes for making the class of substances may be carried out. In the course of the argument, a number of attacks were directed against the specification as a whole, these being predicated on a construction of the specification as purporting to disclose a single invention of processes for the making of the whole class of substances all, or substantially all, of which must, if the patent is to be supported, possess novelty and utility. The plaintiff, however, submitted that as a matter of construction the specification discloses two inventions, one relating to the class of substituted morpholines and the other relating to the single substance 2-phenyl-3-methylmorpholine, and it will, I think, be desirable to determine this question before approaching the question of construction of the specification in detail.

The present specification is in many respects similar to the unamended specification considered in *Re May & Baker Ltd. et al.*[1], but unlike the unamended specification in that case, it does not end with the claims to processes for the making of the whole class of substances and the substances when produced by such processes, but contains in addition a claim to 2-phenyl-3-methylmorpholine (which is one of the members of the class) when made by the processes of claims 1, 2 or 3 or an obvious chemical equivalent. In *Re May & Baker Ltd. et al.*, the specification described an invention relating to a large class of substances and contained claims for processes for their manufacture and for the substances when produced by such processes. The activities of two members of the class were described in the specification as examples of what the substances of the class would accomplish. The specification having been attacked, an application was made for leave to amend it by eliminating the claims as stated in it and substituting therefor a single claim for the two particular substances

[1] (1948) 65 R.P.C. 255.

and by revising the disclosure so as to make it relate only to the two particular substances. This application was refused on the ground that the proposed amendments would make the specification one for a substantially different invention from that claimed in the unamended specification. It is to be observed that neither the unamended specification nor the specification if amended as proposed would have been precisely similar to that of the patent here in suit. However, in support of his argument that the proposed amendment would not make the specification claim an invention substantially different from that claimed in the unamended specification counsel for the patentee in *Re May & Baker Ltd. et al.* in all three courts urged that without changing a single word in it the unamended specification might have included an additional claim for the two particular substances and that if the specification had included such a claim there would be no serious question as to his client's right to disclaim the broad claims and retain the claim for the two substances only. Such a specification would have been almost precisely similar in principle to that in the present case. Referring to the argument so put forth, Jenkins J. said[1] at p. 294, line 40:

> Mr. Drewe strongly contended that the amendments would not make the invention claimed substantially different. He placed great reliance on the fact that the two specific substances to which the amended specifications is reduced are the two given as examples in the unamended specification. These he said (in effect) were the pith or kernel of the invention claimed by the unamended specification and were proved substances of great therapeutic utility, and in retaining them as the sole subject of claim the specification as amended could not be said to claim a substantially different invention merely because it excluded the rest of the numerically very large range of substances falling within the scope of the invention as originally claimed.
>
> According to his argument it was merely a question of restricting the area of application of the invention to the two proved substances and making it what he called "gilt edged"; and he pointed out with force that the two proved substances could actually have been made the subject of a separate claim in the unamended specification without altering a word in the body of that document.

At p. 298, line 8, he continued:

> The amendments alter, as it were, the whole centre of gravity by making the characteristics peculiar to the two specific bodies, which for the purposes of the invention as originally claimed were merely incidental matters, become the very pith and essence—the be-all and end-all—of the invention itself.

[1] (1948) 65 R.P.C. 255.

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Mr. Drewe's argument that the two specific bodies might have been made the subject of a separate claim is, I think, met by the short answer that if they had been it might have been contended that the specification claimed, as in effect a distinct invention, the two specific bodies on the strength of their own exclusive and peculiar characteristics and virtues.

Dealing with the same argument in the Court of Appeal[1], Lord Greene, M.R., said at p. 15, line 19:

> It is said by Mr. Drewe on behalf of the Appellants that the fact that the two specific compounds to which it is proposed to limit the invention are in fact mentioned in the original specification makes all the difference, and that it would have been possible in the original specification to have made them the subject matter of a separate claim.
>
> With regard to this last argument, *I am not by any means satisfied that the suggested separate claims would have been permissible.* This was a Convention patent, and it may well be that the inclusion of such additional claims would have made the patent vulnerable on the ground of disconformity; but, apart from this, as the learned judge points out, *the question would still have arisen whether the inclusion of the two separate claims would not have been in respect of inventions different from the invention which was in fact claimed in the original specification.* That invention relates to a whole genus, each member of which was described as having important therapeutic qualities. The inventive step consisted in the discovery of this common characteristic in the genus. The inventor is telling the public: Make any one of these new substances that you choose: you will find that in every case the promised therapeutic result will follow. This was what was asserted. For the purpose of comparing the invention claimed with that claimed by the amended specification it is immaterial that (as the fact was) the assertion could not be supported. It formed the basis of the invention claimed. The supposed discovery was, however, no discovery at all. It was at best an unproved hypothesis. No such common characteristic existed in all members of the genus. The inventor, however, proceeds to refer to two compounds, namely, those to which the proposed amendment is confined. He refers to these two compounds not as being what in fact they were, discoveries quite independent of the correctness or otherwise of the major proposition, that is, the proposition that all the "new" compounds possessed the alleged characteristics. He describes them as both examples and proofs of the major proposition. He is not saying: "I have discovered by using the experimental method that two compounds have important therapeutic qualities." He is saying: "My discovery is that the whole genus has the stated characteristics and I have proved that this discovery is what I say it is by experimenting with two of the large range of compounds included in the genus." *In other words, the two compounds and the discovery of their therapeutic qualities are not claimed as the invention in the original specification.* They are given merely as examples or proofs of the results said to be obtainable from every member of the genus. *Once the two named compounds, which in the context of the original specification are given a role of a strictly limited character, are taken from their context and converted into a separate independent and self-sufficient invention, they assume, as it appears to me, a quite different character. They are no longer examples or proofs of anything but themselves. They become an invention arrived at by a different*

[1] (1948) 66 R.P.C. 8.

mental process; and the inventive step required to discover their characteristics is entirely divorced from the discovery of the characteristics of the genus from which, according to the original specification, their characteristics are derived. The elimination of the major proposition, and the elevation of the two named substances to an independent status in no way dependent upon or connected with the comprehensive discovery previously alleged, namely the discovery of a quality common to every member of the genus, appears to me to make the amendment proposed something qualitatively different from a mere disclaimer, and the invention which it claims substantially different from that claimed by the original specification.

Mr. Drewe's argument is really based on what he says would have been the result if separate claims for the two named compounds had been included in the original specification. *The addition of such claims, if indeed it would have been permissible, would not, I think, have led to the result which he asserts, having regard to the description of the inventive step contained in the original specification;* but no such claims were in fact included, and we have to construe the specification as it stands, not as it would have stood if it had been cast in a different form. The nature of the invention, and of the relationship to it of the experimental results obtained from the two named compounds being, as I find, what I have stated them to be, *I cannot allow my conclusions to be affected by an* imaginary addition to the original specification *which might have led to a different construction. The document falling to be construed would have been a different document.*

In the House of Lords[1], Lord Simmonds also referred to the same argument at p. 34, line 1 of R.P.C., as follows:

My Lords, I do not think that the Appellants get any help from this somewhat tentative observation. In the first place, as I have already pointed out, no claim was made for the two specific drugs and no explanation was offered why a patentee, who was by no means *inops consilii,* did not make it. In the second place it is a sheer begging of the question to say that in this case "the claims could originally have been separated up without difficulty", if by that is meant that the *Comptroller,* having the knowledge of this art and of the facts which this case has disclosed, *ought to have treated the invention of a group having a general therapeutic value as the same thing as the invention of a specific drug having a particular therapeutic value, and ought accordingly to have granted one patent to cover them both. I am clearly of opinion that he ought to have done no such thing.* I do not ignore that the *Comptroller,* not knowing what was now known, might have granted such a patent, and that in that case there might be the specific as well as the general claim, and, further, that in that case Sec. 32A of the Act might in the event of an infringement action, create a position of peculiar difficulty. But it is not a hypothetical difficulty that has to be faced, and I decline to test the validity of the Appellants' case by creating it.

Lord Normand said at p. 37, line 36:

It was said for the Appellants that this was "mere draftsmanship", an error of omission which could be rectified by supposing that such a claim had been made, and that the specification might be construed as if it contained the claim. *Specifications like other documents must be*

[1] (1950) 67 R.P.C. 23.

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construed as they are, not as they might have been. The absence of a claim of this particular kind, which is almost a matter of style where it is appropriate, cannot be dismissed as a negligible inadvertence. *The addition of a claim for the two specific substances would involve the recasting of the specification, for the claim would not fit the character of the invention asserted in it as it stands.* That invention is a generic invention in which the utility is a generic property invariably associated with the chemical characteristics of the genus. It is really not possible to read the specification as a compendious manner of claiming a vast number of substances, each of which has been found to have therapeutic virtue, and of claiming among them the two specific substances as especially satisfactory or effective examples. Such a claim if made would be rejected by the least sceptical of qualified addressees as a gross and palpable falsehood.

Lord MacDermott also referred to the argument at p. 52, line 21. He said:

It was said that if the original specification has included a claim limited to the two named drugs the amendment now sought would necessarily have been within the power of the Court to grant under Sec. 22 for, as it was put, one could always "amend down" so as to shed all but a narrow claim to the preferred embodiment. If the views I have already expressed as to the nature of the inventive steps underlying the amended and original specifications are well founded this argument, in my opinion, really begs the question and can lead nowhere. The process of amending down to which reference is made does not, as I understand it, involve any change in the nature of the inventive step which remains intact and available to support the narrow claim. But that is not the position here, for *the amendment sought is based on a different inventive step,* and the issue of competence arises directly and must be settled according to the terms of Sec. 22.

In my opinion, the passages I have quoted support the view that a claim for a single substance appended to a disclosure purporting to relate only to the invention of a genus or class of substances should not have been allowed in view of s. 38(1) of the *Patent Act* because two different inventions or alleged inventions would be involved. But whether or not claim 8 should have been allowed in the patent here in question, as issued, the same subsection provides that no objection merely on the ground that the patent has been granted for more than one invention can succeed. Accordingly, as I view the matter, it becomes necessary because of the presence of claim 8 to read the specification not only to see what it says that refers to and describes an alleged invention of processes for the preparation of the class of substances but also to see what, if anything, it says that refers to and describes an invention of 2-phenyl-3-methyl morpholine and processes for its production. For, if the

requirements of s. 36 of the *Patent Act* in respect of the description, etc., of the invention of 2-phenyl-3-methylmorpholine are complied with, the mere fact that the required information is mixed with and included as part of the description of another alleged invention will not by itself render claim 8 invalid. The problem of so reading the specification is embarrassing for by its context the disclosure throughout suggests one and only one invention. But, as a matter of construction of the specification, this suggestion of the specification must, I think, give way in order to give meaning to the specification as a whole which includes claim 8 and thus indicates that besides the invention of the class an invention of the single substance, 2-phenyl-3-methylmorpholine is involved in the disclosure.

The specification commences as follows—omitting immaterial details:

BE IT KNOWN THAT OTTO THOMÄ HAVING MADE AN INVENTION ENTITLED:

PROCESS FOR THE PRODUCTION OF SUBSTITUTED MORPHOLINES

THE FOLLOWING DISCLOSURE CONTAINS A CORRECT AND FULL DESCRIPTION OF THE INVENTION AND OF THE BEST MODE KNOWN TO THE INVENTOR OF TAKING ADVANTAGE OF THE SAME.

THE PRESENT INVENTION RELATES TO A PROCESS FOR THE PRODUCTION OF SUBSTITUTED MORPHOLINES.

Next, after stating that such processes involving the treatment of diethanolamines, e.g. with 70 per cent. sulphuric acid at 160-180°C, are already known but that it is particularly necessary, when producing substituted morpholines, to find specially mild reaction conditions for the ring closure and that there is danger of undesired side reactions which can be brought about by the influence of temperature or the acids employed for the ring closure, it proceeds to say:

THE OBJECT OF THE PRESENT INVENTION IS THEREFORE A PROCESS, ACCORDING TO WHICH THE RING CLOSURE LEADING TO MORPHOLINE DERIVATIVES CAN BE CARRIED OUT UNDER PARTICULARLY MILD REACTION CONDITIONS, e.g. WITHOUT ADDITIONAL HEATING OR WITH ONLY SLIGHT HEATING.

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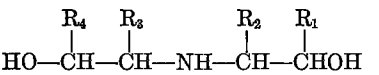
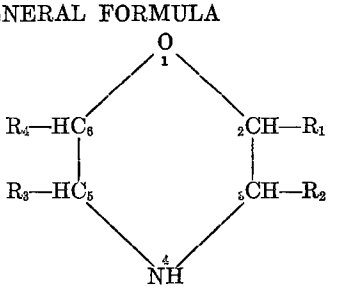
It next contains the statements already referred to about U.S. Letters Patent 2,566,097 but that generally vigorous conditions are necessary and continues:

IT HAS NOW SURPRISINGLY BEEN FOUND THAT A CERTAIN GROUP OF SUBSTITUTED DIETHANOLAMINES OF THE GENERAL FORMULA

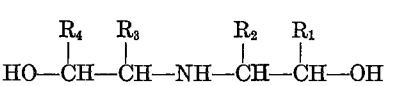


WHEREIN R_1 IS A PHENYL RESIDUE, WHICH IF DESIRED CAN BE SUBSTITUTED BY A HYDROXYL GROUP OR A LOW MOLECULAR ALKYL- OR ALKOXY RESIDUE, R_2 AND R_3 ARE HYDROGEN ATOMS OR PHENYL- OR ALKYL RESIDUES AND R_4 IS A HYDROGEN ATOM OR A PHENYL RESIDUE, CAN BE SUBJECTED TO THE MORPHOLINE RING CLOSURE UNDER PARTICULARLY MILD CONDITIONS AND WITHOUT DISTURBING SIDE-REACTIONS.

THEREFORE, THE PRESENT INVENTION RELATES TO A PROCESS FOR THE PRODUCTION OF SUBSTITUTED MORPHOLINES OF THE GENERAL FORMULA



WHEREIN R_1 TO R_4 HAVE THE ABOVE-NAMED MEANINGS. ACCORDING TO THE INVENTION THE SUBSTITUTED MORPHOLINES OF THE SAID GENERAL FORMULA ARE PRODUCED BY INTRODUCING SUBSTITUTED DIETHANOLAMINES OF THE GENERAL FORMULA



WHEREIN R_1 TO R_4 HAVE THE ABOVE DEFINITIONS, WITHOUT HEATING INTO CONCENTRATED (96%) SULPHURIC ACID OR BY TREATING THEM WITH DILUTED ACIDS AT MODERATE TEMPERATURES.

It will be observed that, up to this point, there has been no indication beyond that contained in the title and in the clause stating the object of the invention as to what the alleged invention is. It has, however, been stated that the object of the invention is a process according to which the morpholine ring closure can be carried out under particularly mild reaction conditions, *e.g.* without heating or with only slight heating (cooling is also mentioned later) and that,

according to the invention, the substituted morpholines are produced by introducing substituted diethanolamines of the general formula already mentioned without heating into concentrated (96 per cent.) sulphuric acid or by treating them with diluted acids at moderate temperatures. As I read the specification, moderate reaction temperatures are thus a characterizing feature in what is being described and a second feature of what is being described is that the morpholine ring closure is brought about by the treatment of the substituted diethanolamine with acid. Nor is this impression dispelled by what follows wherein for the first time salts of the diethanolamines, as well as the bases, are mentioned. The disclosure proceeds:

IF THE RING CLOSURE IS PRODUCED WITH CONCENTRATED SULPHURIC ACID WITHOUT HEATING, THEN, USING THE FREE BASE AS STARTING MATERIAL IT WILL BE CONVENIENT TO WORK UNDER GOOD COOLING CONDITIONS ON ACCOUNT OF THE HEAT OF NEUTRALIZATION. HOWEVER, ONE CAN ALSO START FROM A SALT OF THE BASE, WHICH CAN BE INTRODUCED INTO THE CONCENTRATED SULPHURIC ACID WITHOUT SPECIAL COOLING. THE DESIRED MORPHOLINE DERIVATIVE HAS FORMED AFTER SEVERAL HOURS STANDING AND CAN BE WORKED UP IN THE USUAL MANNER, e.g. BY POURING ON ICE, MAKING ALKALINE AND EXTRACTING WITH ETHER AND PURIFYING THE MORPHOLINE BY CRYSTALLIZATION OR DISTILLATION.

WHEN WORKING WITH DILUTED ACIDS THE REACTION RESULTS, AS ALREADY MENTIONED ABOVE, LIKEWISE UNDER RELATIVELY MILD CONDITIONS. IN MANY CASES IT IS SUFFICIENT TO OPERATE AT ROOM TEMPERATURE. WITH OTHER DERIVATIVES GENTLE WARMING OR HEATING TO WATERBATH TEMPERATURE WITH AN AQUEOUS OR ALCOHOLIC ACID IS NECESSARY. THIS PROBABLY DEPENDS ON THE TYPE OF SUBSTITUTES. THE ACTUAL REACTION CONDITIONS CAN EASILY BE ASCERTAINED BY SIMPLE PRELIMINARY TESTS. AS DILUTE ACIDS, WHICH MAY BE USED IN THE PROCESS ACCORDING TO THE INVENTION CAN BE MENTIONED BY WAY OF EXAMPLE: SULPHURIC ACID, HYDROBROMIC ACID, HYDROCHLORIC ACID, ETC.

It should be observed that the expression "the desired morpholine" refers in the same sentence to a salt and to the base, for it is a salt of the morpholine which has formed after several hours but what is worked up by making alkaline is the base. In the context, however, and having regard to the general formula of the class of morpholine the reference to the fact that the desired morpholine can be worked up

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by making alkaline, in my opinion, indicates that the purpose of the process which is being described is to produce the base rather than any of the numerous salts.

The specification next contains a paragraph suggesting a preferred way of preparing the diethanolamine starting material which, it should be noted, is a method of preparing the base rather than any salt, and then proceeds to say:

> THE MORPHOLINES PRODUCED ACCORDING TO THE INVENTION ARE VALUABLE PHARMACEUTICALS OR INTERMEDIATE PRODUCTS FOR THE PRODUCTION OF PHARMACEUTICALS. (I pause to observe that this suggests that the invention—whatever it may be—is not the morpholines, since they are something produced "according to the invention" and are not even referred to as being new substances). THE PHARMACOLOGICAL BEHAVIOR OF THE COMPOUNDS OBTAINED ACCORDING TO THE PRESENT INVENTION, WILL BE MORE FULLY DESCRIBED BY THE EXAMPLE OF ONE OF THE COMPOUNDS OF THIS CLASS, THE 2-PHENYL-3-METHYLMORPHOLINE. THE MOST IMPORTANT EFFECT OF SAID SUBSTANCE APPEARS WHEN COMPARED WITH BENZEDRINE (PERVITINE) TO WHICH IT IS SUPERIOR INASMUCH AS IT CAUSES THE PARTICULARLY DESIRED EFFECT OF DEFERRING THE TIRING WHILST BEING LESS POISONOUS AND LESS STIMULATING.

This is followed by comparative data respecting the toxicity, the stimulating effect of the substance and its effect on blood pressure and a paragraph of information as to its effects and advantages when administered to humans. The paragraph ends with the sentence:

> THE OTHER COMPOUNDS OF THIS CLASS WILL PRODUCE SIMILAR EFFECTS.

Next in order come ten examples which are introduced by the sentence:

> THE FOLLOWING EXAMPLES WILL MORE CLEARLY EXPLAIN THE INVENTION, WITHOUT LIMITING IT.

Of the examples, numbers 1, 2, 3, 4 and 10 are all carried out with concentrated sulphuric acid at room temperature. In 1, 2, 3 and 4, the starting materials are all diethanolamine hydrochloride salts, while in number 10 the starting material is a base. Number 5 is also an example of the use of concentrated sulphuric acid with a base. In it, the temperature is said to rise to 40° because of the heat generated by the neutralization, and it is then left to react at room temperature. Examples 6, 7, 8 and 9 are the only examples of the use of dilute acids. Of these, number 6 relates to the use of 30 per cent. sulphuric acid at water bath temperature, number 7 to 5 per cent. hydrochloric acid at boiling temperature, number 8 to hydrogenation in methanol at room temperature, and number 9 to 10 per cent. hydrochloric acid

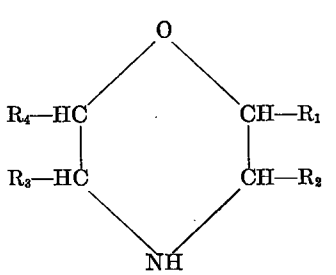
at water bath temperature. Examples 2 and 9 relate to the preparation of 2-phenyl-3-methyl morpholine, the starting material in each case being the hydrochloride salt of B-phenyl-α-methyl-B,B[1]-dihydroxy-diethylamine. In all examples except number 8, a method of neutralizing the product of the reaction to form the substituted morpholine bases is referred to, and in all but 5 and 10 preparation of the hydrochloride salt from the base is also described or referred to.

To recapitulate, the facts descriptive of the invention which have been made to appear thus far are that it is entitled a process for the production of substituted morpholines, that it relates to a process for the production of substituted morpholines, that its object is a process according to which the ring closure of diethanolamines to form morpholine derivatives can be carried out under particularly mild reaction conditions, that since it has been found that a certain large group of substituted diethanolamines can be subjected to the ring closure under particularly mild reaction conditions without disturbing side reactions it (the invention) relates to a process for the production of substituted morpholines of that class, that according to it (the invention) such substituted morpholines are produced by introducing substituted diethanolamines of a certain class without heating into concentrated sulphuric acid or by treating them with diluted acids at moderate temperatures and that the morpholines produced according to the invention are valuable pharmaceuticals or intermediate products for the production of pharmaceuticals and all of them will produce effects similar to those described as the effects of 2-phenyl-3-methylmorpholine.

The remainder of the specification is as follows:

THE EMBODIMENTS OF THE INVENTION IN WHICH AN EXCLUSIVE PROPERTY OR PRIVILEGE IS CLAIMED ARE DEFINED AS FOLLOWS:

1. PROCESS FOR THE PRODUCTION OF SUBSTITUTED MORPHOLINES OF THE GENERAL FORMULA



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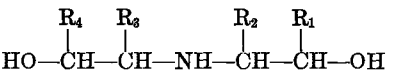
WHEREIN R_1 IS A PHENYL RESIDUE, OR A PHENYL RESIDUE SUBSTITUTED BY HYDROXYL, LOWER ALKYL, OR LOWER ALKOXY, R_2 AND R_3 ARE HYDROGEN ATOMS OR PHENYL OR ALKYL RESIDUES AND R_4 IS A HYDROGEN ATOM OR A PHENYL RESIDUE, CHARACTERIZED IN THAT DIETHANOLAMINES OF THE GENERAL FORMULA



WHEREIN R_1 TO R_4 HAVE THE ABOVE MEANING, ARE TREATED IN THE PRESENCE OF ACIDS.

2. PROCESS ACCORDING TO CLAIM 1, CHARACTERIZED IN THAT THE RING CLOSURE IS BROUGHT ABOUT WITH CONCENTRATED SULPHURIC ACID WITHOUT HEATING.

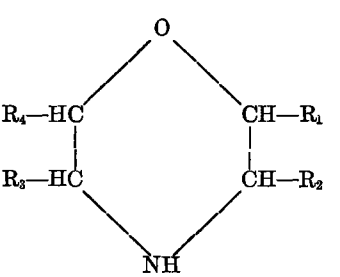
3. PROCESS ACCORDING TO CLAIM 2, CHARACTERIZED IN THAT USING THE FREE BASE AS STARTING MATERIAL ONE OPERATES WITH COOLING.

4. PROCESS ACCORDING TO CLAIM 2, CHARACTERIZED IN THAT WHEN USING A SALT OF THE SUBSTITUTED DIETHANOLAMINE AS STARTING MATERIAL ONE WORKS AT ROOM TEMPERATURE.

5. PROCESS ACCORDING TO CLAIM 1, CHARACTERIZED IN THAT THE RING CLOSURE IS BROUGHT ABOUT BY WORKING WITH DILUTED ACIDS AT TEMPERATURES BELOW 100°C.

6. PROCESS ACCORDING TO CLAIM 5, CHARACTERIZED IN THAT SULPHURIC ACID, HYDROBROMIC ACID OR HYDROCHLORIC ACID ARE USED AS DILUTED ACID.

7. MORPHOLINE DERIVATIVES OF THE GENERAL FORMULA



WHEREIN R_1 IS A PHENYL RESIDUE, WHICH MAY BE SUBSTITUTED BY A HYDROXYL GROUP OR A LOW MOLECULAR ALKYL OR ALKOXY RESIDUE, R_2 AND R_3 ARE HYDROGEN ATOMS OR PHENYL OR ALKYL RESIDUES AND R_4 IS A HYDROGEN ATOM OR A PHENYL RESIDUE, WHEN PREPARED BY THE PROCESS OF CLAIM 1, 2 OR 3, OR BY AN OBVIOUS CHEMICAL EQUIVALENT.

8. 2-PHENYL-3-METHYLMORPHOLINE, WHEN PREPARED BY THE PROCESS OF CLAIM 1, 2 OR 3, OR BY AN OBVIOUS CHEMICAL EQUIVALENT.

It will be noted that, while claims 2, 3, 4 and 5 are all process claims wherein temperature conditions—none of which exceed 100°C—are specified, claim 1 purports to embrace the process of treating any diethanolamine of the class therein defined in the presence of any acid, concentrated or dilute, with no limitation whatever on the temperature at which the reaction is to be carried out. This may be contrasted with the disclosure which says that "according to the invention the substituted morpholines of the said general formula are produced by introducing substituted diethanolamines of the general formula . . . without heating, into concentrated (96%) sulphuric acid or by treating them with diluted acids at moderate temperatures". The process claimed in claim 1 is thus broader than the process described in the disclosure in that, while according to the latter the diethanolamines are introduced without heating into concentrated sulphuric acid or treated with diluted acids at moderate temperatures, the former is a process wherein concentrated acids other than concentrated sulphuric acid may be used and which when using either concentrated or diluted acid may be carried out at temperatures which are other than moderate.

It should also be noted that while claims 2, 3 and 4, and probably 5 and 6 as well, are limited to processes in which the ring closure is produced by the action of the acid on the diethanolamine, the process of claim 1 is not so limited and a process of producing a ring closure by the reaction of any other substance on a diethanolamine of the class would fall within claim 1 if it were carried out in the presence of acid.

Finally, it should be noted that provided a substituted morpholine of the defined class is produced by the treatment of a substituted diethanolamine of the defined class in the presence of acid, claim 1 will cover the process even though the substituted morpholine so produced may not be that of the corresponding substituted diethanolamine because of re-arrangement of the positions of the substituents having occurred in the process.

Turning now more particularly to what the specification says about 2-phenyl-3-methylmorpholine, the first specific reference to this substance appears in the opening paragraph of p. 5 which reads:

> The morpholines produced according to the invention are valuable pharmaceuticals or intermediate products for the production of pharmaceuticals. The pharmacological behavior of the compounds obtained

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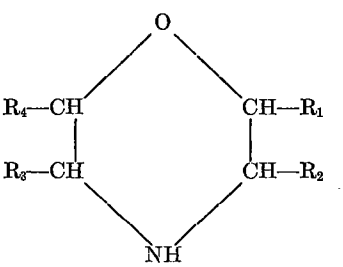
according to the present invention, will be more fully described by the example of one of the compounds of this class, the 2-phenyl-3-methylmorpholine.

This is followed by data purporting to state the effects of "the said substance". It is to be noted, however, that the expression "the said substance" refers to 2-phenyl-3-methylmorpholine as "the example of one of the compounds of this class" which in turn refers to "the compounds obtained according to the present invention". "The present invention" thus far referred to related to a process for the preparation of substituted morpholines of the class represented by the general formula



and according to it, they were produced by introducing substituted diethanolamines of the general formula mentioned without heating into concentrated (95°) sulphuric acid or by treating them with diluted acid at moderate temperature, etc. It is thus only 2-phenyl-3-methylmorpholine when produced by these processes that is being described. Nor do I think that the 2-phenyl-3-methylmorpholine which is thus referred to is to be divorced from the process and conditions described. It is not to be assumed that the specification does not mean precisely what it says and it is to be borne in mind that the substance had not been previously made or used. The specification itself has already warned of the danger of undesired side reactions which may be brought about by the influence of the temperature and the acid used, and it appears from the evidence that there are two stereo isomeric forms of the 2-phenyl-3-methylmorpholine molecule, and that it is the formation of the trans isomer which is favoured in the reaction as described in the specification. The properties and pharmacological effects of the substance described in the specification are thus presumably ascribable to the trans isomer. As the substance had not previously been made, it may not have been predictable at the time

that more vigorous conditions would not result in formation of the products of undesired side reactions or of the cis isomer of 2-phenyl-3-methylmorpholine in greater proportion, either of which might contaminate the result so as to render the process under such conditions useless or less useful than the restricted process which was being described. Having regard to this as well as to the duty of the patentee to correctly and fully describe his invention, I would construe the reference to 2-phenyl-3-methylmorpholine produced according to the invention as a deliberate limiting of the description of the substance to that substance when produced under the moderate temperature conditions which had already been outlined.

The paragraph referred to is followed by those which give detailed data concerning the action or effects of the 2-phenyl-3-methylmorpholine so prepared and then in examples 2 and 9 two processes for producing it are described in some further detail. Example 2 is a process by which the 2-phenyl-3-methylmorpholine is prepared by dissolving B - phenyl-α-methyl-B,B1-dihydroxy-diethylamine-hydrochloride in concentrated sulphuric acid, allowing it to stand overnight at room temperature, subsequently making the reaction material alkaline with caustic soda and then extracting the 2-phenyl-3-methylmorpholine. The substance so obtained is said to be a liquid which boils at 138°C. It is then mentioned that the hydrochloride crystallizes from alcoholic hydrochloric acid and acetone and has a melting point of 182°C. Example 9 which is headed "2-phenyl-3-methylmorpholine" refers to a process of warming the same diethanolamine hydrochloride with 10 per cent. hydrochloric acid for six hours on a water bath and states that "after working up in the usual manner (which in my opinion means making basic and extracting), the hydrochloride of the 2-phenyl-3-methylmorpholine crystallizes out from methanolic hydrochloric acid and acetone". In my opinion, one possible reason for mentioning this salt is that if taken orally in small quantity it would have the same effect as the base. It is notable that the salt of no other acid is mentioned in the same way in this or any of the other examples. A second reason may be that in this example as well as in each other example when the hydrochloride salt is similarly mentioned, the salt is a solid with a melting point above 100°C which may be a desirable characteristic

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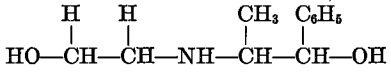
if the substance were to be stored for some time. But whether these are the reasons or not why the hydrochloride salts of these 9 substituted morpholines are so mentioned, I can see in the fact that they are mentioned in examples which are headed by the name of the substituted morpholine no sufficient reason for thinking that the author of the specification was using the names of these morpholines loosely to refer either to the morpholine itself and its hydrochloride salt or to the morpholine itself and all its salts. What follows in the specification with relation to 2-phenyl-3-methylmorpholine is simply the wording of claim 8 and claims 1, 2 and 3 to which claim 8 refers.

With respect to the product aspect of claim 8, it was contended on behalf of the plaintiff that the name 2-phenyl-3-methylmorpholine should be construed as embracing the substance 2-phenyl-3-methylmorpholine and all its salts when prepared by the processes mentioned. In this connection, it may be noted that the processes of claims 1, 2 and 3, so far as they are detailed in the claims, are confined to the treatment of diethalomines of the class in the presence of acids which initially would produce the morpholine salt of the acid used. But this consideration in my opinion is outweighted by other features of the specification. The whole tenor of the disclosure is to describe the making of the substituted morpholines and this term in its proper and common usage refers to the morpholine bases and not to their salts. Further, the salts of the morpholines are different substances from the morpholines themselves, having structural and empirical formulas which differ from those of the morpholines. The morpholine molecular structure is given in the disclosure and in the claims, but the structure of a morpholine salt is nowhere to be found in either the disclosure or the claims. Moreover, the information given in the disclosure regarding the pharmacological effects of the use of 2-phenyl-3-methylmorpholine are, as I read the specification in relation to this invention, the effects of that single substance. Its salts are not referred to as having such effects and to read claim 8 as including them would be to extend it to substances for which, as I read the specification, no pharmacological utility had been asserted and some if not most of which would be unlikely to have any useful pharmacological activity. Moreover, there is no indication in the evidence that any but a small number of these, out

of the thousands which would make up the class of such salts, has ever been made. I am accordingly of the opinion that as a matter of construction the name 2-phenyl-3-methylmorpholine in claim 8 refers to the base only having that name and does not include any salt of that base.

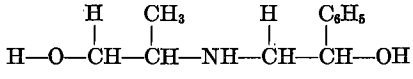
Turning now to the process aspect of the claim, it was contended on behalf of the plaintiff that for the purposes of this case, claim 8 should be read as saying

2-phenyl-3-methyl morpholine, when prepared by a process characterized in that a diethanolamine of the formula



is treated in the presence of acids or by an obvious chemical equivalent.

I am not satisfied that claim 8 is so limited for I do not see how it could, as stated in the patent, be said to exclude 2-phenyl-3-methylmorpholine when produced by treating other diethanolamines of the class in the presence of acids as, for example, if it could be produced by treating a diethanolamine of the formula



in the presence of acids. The fact of the matter is that claim 1 is a claim relating to the alleged invention of the class. It is not a claim in respect of the other invention, i.e. of 2-phenyl-3-methylmorpholine, and it does not fit that invention.

But even assuming that claim 8 can be read as narrowly as suggested by counsel for the plaintiff, it still claims the substance 2-phenyl-3-methylmorpholine whenever prepared by treating the particular diethanolamine in the presence of any acid, whether concentrated or dilute, and at any temperature, whether moderate or not. In these respects, the process aspect of claim 8 as so worded would be coextensive with that of claim 1 in so far as it relates to the treatment of the particular diethanolamine. It would, however, not be coextensive with, but broader in scope than the process for making the class of morpholines of which 2-phenyl-3-methylmorpholine is one, which is described in the disclosure

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for, according to that process, the diethanolamine is introduced without heating into concentrated sulphuric acid or is treated with diluted acid at a moderate temperature. It would also be broader than the process as disclosed in that it would embrace the bringing about of the morpholine ring closure by the action of some other substance on the diethanolamine provided only that it were carried out in the presence of acid.

I turn now to the objections to validity raised in the course of argument on behalf of the defendant. These were put forward in three groups, the first group being directed against the patent as a whole, the second group against claim 8, and the third group, which is really a sub group of one of the objections in the second group, against claim 1. The objections raised in the first group were all based on the defendant's submission that the patent related to one invention only, that one being a process for the production of the whole enormous class of substances and on this basis three objections were urged. First, it was said that not all members of the class were useful and the invention as claimed lacked utility. Secondly, it was argued that the patent is a selection patent in that the inventor has selected as starting materials diethanolamines, having certain characteristics and particular reaction conditions and that the patent does not comply with the requirements for a patent for an invention of this kind because in such a case the starting materials must all be capable of producing useful products which is not the fact and because the reaction referred to can in fact be carried out under conditions other than those selected. The third of this group of objections was that with regard to the process as described wherein dilute acids are to be used, the patent leaves it to the public to experiment to find out how it works. As I have reached the conclusion that the specification purports to disclose more than one invention, it becomes unnecessary to deal with these particular objections. Some of them, however, were raised as well with respect to the invention of 2-phenyl-3-methylmorpholine and one of them is referred to in connection with the objections to claim 1.

The second group of objections—all to claim 8—consisted in substance of four separate objections and it will be convenient to deal with these in turn as they are stated though not necessarily in the order in which they were presented.

The first of these objections was that even if claim 8 is for a second invention, 2-phenyl-3-methylmorpholine was not shown to have greater pharmacological value to a sufficient extent over known drugs to support a claim to an invention and that any advantage it may have over these was within the realm of what could be expected of this substance when made. In the defendant's submission, in order to support the claim, it would be necessary to obtain affirmative answers to two questions, the first of which counsel referred to as the pre-Cripps question and the second as the Cripps question. In suggesting these questions, counsel referred to the judgment of Jenkins J. in *Re May & Baker Ltd. et al.*[1], and by way of explanation of the submission, it may be useful to quote at this point some passages from the judgment in that case. At p. 281, line 14, Jenkins J. said:

> Before referring to this evidence, I should, I think, endeavour to state the principles on which, and limits within which, an invention consisting of the production of new substances by known methods from known materials can be supported from the point of view of subject-matter. I understand them to be these:—
>
> (i) An invention consisting of the production of new substances from known materials by known methods cannot be held to possess subject-matter merely on the ground that the substances produced are new, for the substances produced may serve no useful purpose, in which case the inventor will have contributed nothing to the common stock of useful knowledge (the methods and materials employed being already known) or of useful materials (the substances produced being, *ex hypothesi,* useless).
>
> (ii) Such an invention *may,* however, be held to possess subject-matter provided the substances produced are not only new but useful, though this is subject to the qualification that the substances produced must be truly new, as opposed to being merely additional members of a known series (such as the homologues) and that their useful qualities must be the inventor's own discovery as opposed to mere verification by him of previous predictions.
>
> (iii) Even where an invention consists of the production of further members of a known series whose useful attributes have already been described or predicted, it may possess sufficient subject-matter to support a valid patent provided the somewhat stringent conditions prescribed by *Maughham,* J., as he then was, in *I. G. Farbenindustrie A-G's Patents* (47 R.P.C., 289) as essential to the validity of a selection patent are satisfied, i.e. the patent must be based on some substantial advantage to be gained from the use of the selected members of the known series or family of substances, the whole (or substantially the whole) of the selected members must possess this advantage, and this advantage must be peculiar (or substantially peculiar) to the selected group.

[1] 65 R.P.C. 255.

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And at p. 282, line 24:

Applying these principles to the present case, I conclude that the invention as claimed by the unamended specification can be held to possess subject-matter if (but not unless) (*a*) the products of the invention are useful, and (*b*) the utility of the products can (having regard to the state of chemical and chemo-therapeutic knowledge on the relevant date, viz. 31st January, 1938) fairly be described as the inventor's own discovery as opposed to a mere verification of, or obvious corollary to, something previously known. In other words, if the products of the invention as claimed are useful, then there may be subject-matter if an affirmative answer can properly be given to the question put by Mr. *Cripps*, as he then was, in *Sharpe & Dohme v. Boots Pure Drug Coy. Ld.* (*supra*), which in its application to the present case may be paraphrased as follows: "Was it for all practical purposes obvious to any skilled chemist, in the state of chemical and chemo-therapeutical knowledge existing on the 31st January, 1938, that he could produce substances possessing greater chemotherapeutic utility than sulphanilamide by applying to the materials described in the specification (and admittedly known to him either as existing or as theoretically possible bodies) the methods described in the specification (and also admittedly known to him as reactions of general application) so as to produce the new substances claimed?" If, on the other hand, the products of the invention as claimed are not useful, then *cadit quaestio* and the further question does not arise.

As to utility, it is of course obvious that chemotherapeutic utility is the only field of usefulness here in question. Further, as appears from my paraphrase of what was referred to in argument as "the Cripps question", I think that utility here must be considered as a relative term. The starting point is sulphanilamide (para-amino-benzene-sulphonamide), and while the range of products embraced by the invention as claimed is very wide owing to the large variety of further substitutions (both on the sulphanilamide side and on the thiazole side of the synthesis) which is invited or permitted by the terms of the specification, all such products are, broadly speaking, some form or other of thiazole-substituted sulphanilamides. I think it follows that the utility of the products of the invention as claimed in the unamended specification must be measured by reference to the chemotherapeutic value of the simple sulphanilamide and that they cannot be classed as useful for the present purpose except in so far as they may be of greater chemotherapeutic utility (for instance, of greater or more general anti-bacterial activity and/or of less toxicity) than the simple sulphanilamide itself. I apprehend that chemotherapeutic utility could hardly be claimed for an invention comprising the manufacture of a sulphanilamide derivative which for chemotherapeutic purposes possessed no advantage whatever over the parent substance. The question as to utility which must be answered affirmatively before the "Cripps question" arises, can, therefore, I think, be stated as follows:—"Can it be predicated as a general proposition of all the products of the invention as claimed—or of substantially all of such products (for I do not think that a few exceptions would necessarily affect the result)—that they are of greater chemotherapeutic value than the simple sulphanilamide?" In considering the evidence bearing on this question it is important to distinguish between the utility of the products of the invention as claimed by the unamended specification, and the utility of the two specific products (sulphathiazole and sulpha-methyl-thiazole)

given as examples of the invention in the unamended specification, but now sought to be made the whole of the invention by the proposed amendments.

Since in the present case the alleged invention of phenmetrazine (2-phenyl-3-methylmorpholine) was one of a new substance by the application of a known method to a known substance, it was submitted that to determine whether the alleged invention possessed subject-matter it would be necessary to answer first the question, "Can it be predicated that phenmetrazine is of greater pharmacological value than the other four known drugs, viz. amphetamine (also known as benzedrine), nor-ephedrine (also known as propadrine), pervitine and ephedrine?" and then if, but only if, the answer to this question were in the affirmative, a further question would arise similar in substance to the "Cripps question" the form of which was the subject of some argument but which I think would be substantially as suggested by Mr. Robinson, who put it thus, "Was it for all practical purposes obvious to any skilled chemist in the state of chemical and chemotherapeutical knowledge existing on the 30th of June, 1953, that he could produce a substance possessing greater pharmacological utility than the common drugs (amphetamine, norephedrine, pervitine and ephedrine) by applying to the diethanolamine (B-phenyl-α-methyl-B,B^1 dihydroxy-diethylamine) (admittedly known to him as an existing body) the method of treating in the presence of acids (admittedly known to him as a reaction of general application) so as to produce the new substance claimed?"

In view of the *prima facie* presumption in favour of the validity of the patent, I think it must be assumed at the outset that the answer to the first of these questions is "yes" and to the second of them is "no" and that these answers must remain the answers at the end of the proceedings unless by a preponderance of evidence it has been established that either of them is not true.

On the first of these questions, there is first the evidence of Dr. Bernard Belleau, a highly qualified professor of chemistry who has had experience in chemical research and in teaching organic chemistry, biochemistry and various aspects of medicinal chemistry. According to his evidence the four known drugs, amphetamine, nor-ephedrine, pervitine and ephedrine, while all useful to about the same extent

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to produce stimulation and depress appetite also had, to about the same extent, the undesirable effect of raising blood pressure. There were, however, some variations in the extent of the effects produced by these drugs. Comparing the four drugs mentioned with phenmetrazine, the witness said, in cross-examination, p. 646, line 20 to p. 648, line 8:

Q. You mentioned in connection with the activity of these—would it be correct to say that these five compounds fall into a category of drugs that have a similar activity?

A. These five—yes, qualitatively they share many pharmacological properties.

Q. And I think you have three groups which you have indicated in your evidence-in-chief, of effects, and one, I think, was the stimulating effect.

A. The cardiovascular effect.

Q. Yes, the blood pressure effect, and I think you said something which had to do with the effect of eating less?

A. Yes, this has been noted also.

Q. Can you indicate Dr. Belleau, with regard to these five compounds —first of all, would you say all of them have some of these three effects?

A. Yes.

Q. All of them have some of them?

A. I believe so, yes, to varying degrees.

Q. Yes, to varying degrees. I will be coming to that in a minute. I want to try to classify these as to which of the three varying effects is most pronounced in each of them.

A. They vary from each other.

Q. I know they vary from each other, but which of these five, for instance, in your opinion, would you think has the strongest stimulating effect?

A. This is based on my present knowledge, of course?

Q. I beg your pardon?

A. This is based on what I know about these compounds. I would say the four top ones—I believe they are approximately equally efficient as central stimulants, and they all also have approximately similar blood pressure effects. They cause a rise in blood pressure to roughly the same extent. I think these four top compounds do that. Now, it is known that the last one—it seems with respect to this last one that it also has this central stimulating activity but to a much smaller degree, and this blood pressure effect is also known to be—it has been reported to be appreciably less than in those other four.

Dr. Belleau also said that phenmetrazine is used in the treatment of obesity, the desired effect being to depress appetite without the disadvantage of an increase in blood pressure. In addition to the evidence of Dr. Belleau, there is evidence given by Professor Silvano Rossi of a concerted

and lengthy effort on the part of Industria Chimica Profarmaco S.p.A., an Italian corporation engaged in the manufacture of fine chemicals—to find a practical way to produce phenmetrazine as well as evidence of the commercial production and sale of it. To my mind, this evidence rather than indicating a negative answer to the first of the suggested questions weighs in favour of the conclusion that it is properly answered in the affirmative. Nor does the evidence satisfy me that phenmetrazine does not have the advantages which the specification claims for it. According to the specification, "The most important effect of said substance (phenmetrazine) appears when compared with benzedrine (pervitine), to which it is superior inasmuch as it causes the particularly desired effect of deferring the tiring whilst being less poisonous and less stimulating". The specification next proceeds to say that with white mice the LD/50 (lethal dose for 50 out of 100 mice) when subcutaneously injected is 200 milligrams per kilogram of body weight compared with 75 milligrams per kilogram of body weight for benzedrine. Perorally administered the corresponding figures with white mice are 475 mg/kg for phenmetrazine against 95 mg/kg for benzedrine. When injected intraperitoneally with white mice the LD/50 is 200 mg/kg for phenmetrazine compared with 50 mg/kg for benzedrine. The specification then says:

> The stimulating effect on mice and rats, measured by the increase in motility, is approximately 7 to 10 times lower than that of benzedrine.
>
> Effect on blood pressure is about 1000-1500 times lower than that of adrenaline.

Presumably the last sentence quoted would have some meaning to a pharmacologist, but there is no evidence upon which I can assess the extent to which superiority in this respect exists over benzedrine, nor-ephedrine, pervitine and ephedrine. There is thus nothing upon which a finding that phenmetrazine was not in this respect more useful than the other drugs could be founded.

In the specification, there follows a paragraph indicating that phenmetrazine has no effect on blood sugar level and then this paragraph:

> When administered to human beings, dosages up to 25 mg will not cause any disadvantageous effects, but will cause a notable deferring of tiring. Said dosages of the substance will not cause excitation, as does the pervitine, nor will cause abrupt mental processes; on the contrary, an

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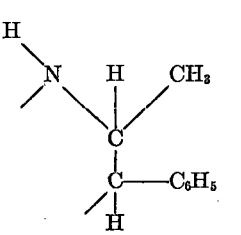
excellent ability of mental concentration will be experienced after administration of the substance. When administrated in larger dosages and parenterally stimulation can be caused as after administration of pervitine; this stimulation however will not be accompanied by a corresponding increase in blood pressure.

An attempt was made to show that on the information so given phenmetrazine would have no advantage as far as toxicity was concerned over benzedrine if the effective dose of the latter substance were 5 mg as against 25 mg for phenmetrazine. This it seems would follow, but the evidence leaves me unsatisfied that 5 mg of benzedrine is the equivalent of a 25 mg dose of phenmetrazine and I would accordingly base no conclusion on the assumption that it was. On the same assumption, it was argued that the claimed advantage of the stimulating effect being 7-10 times lower for phenmetrazine would be reduced to a very small or trivial advantage, but while this may follow as well if the assumption is correct, I can base no finding on it for the reason already stated. Accordingly, while the specification claims for phenmetrazine advantages the extent of which I find it impossible to assess, the evidence does not in my opinion show that phenmetrazine does not possess such advantages in some measure, nor does it show that the measure in which such advantages is possessed is so small as to lead one to say that phenmetrazine is not of greater pharmacological value than the four similar known drugs. The answer to the first (or pre-Cripps) question is accordingly in the affirmative and this brings me to the second (or Cripps) question.

Here again, the *prima facie* answer in my opinion is supported rather than changed by the evidence. It appears that all four of the similar known drugs have as part of their molecular structure what may be referred to as the 1-phenyl-2-amino-propane skeleton which may be depicted thus



The differences in the molecular structure of the four drugs lie in what atoms or groups of atoms occupy the two bonding positions shown as unoccupied in the above structure. The molecule of 2-phenyl-3-methyl morpholine also includes this skeleton. Dr. George F. Wright, a professor of chemistry of outstanding qualifications and with a lifetime of experience in chemical research and teaching, who was called on behalf of the defendant, was able to put the position no higher than that if he had been familiar with the four known similar drugs and had been shown the formula or structure of phenmetrazine he would have expected it would be worthwhile to synthesize it—that the odds would be good "that it would have that activity", or "the odds would be sufficiently good that (he) would be willing to make the synthesis". It is, I think, fair to note that if the substance to be so synthesized were to exhibit the hoped for activity at all, the probability was that such activity would vary in some respects from those of the four known drugs. But this, to my mind, is far from suggesting that it was predictable that 2-phenyl-3-methylmorpholine would possess advantages over the four known drugs. The evidence shows that there are some 200 known substances which include the 1-phenyl-2-amino-propane skeleton in their molecular structures of which about 30 are known to have pharmacological activity while the rest do not, and a myriad of other conceivable substances embracing this skeleton which have never been made and of which the pharmacological activities are not predictable. I see no reason to think that what might have been hoped for with respect to phenmetrazine could not for the same reason have been hoped for from a large number of the compounds and conceivable compounds which embrace this skeleton and yet it appears that most of the known compounds having it do not have pharmacological value. Moreover, the opinion of Dr. Wright as so expressed assumes that for some reason, 2-phenyl-3-methylmorpholine has already been selected from the myriad of unknown but conceivable compounds as suitable for consideration which, I think, distorts the problem as it would have presented itself to one who knew about the four drugs and embarked on the task of making a new substance of greater value for pharmacological purposes. To such a person, it would no doubt occur to explore substances having the 1-phenyl-2-amino-propane skeleton and even within that class it might

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be easy to eliminate sizable groups as being too difficult to prepare or too unlikely because of the size of the molecule to exhibit the desired activity, but after this was done there would still remain a large group of possible substances from which to choose those suggesting the best possibilities and it would only be at this stage, if 2-phenyl-3-methylmorpholine was within a group thought worthy of examination that the question as presented to Dr. Wright would have arisen. Moreover, Dr. Wright spoke from the point of view of a chemist rather than a pharmacologist and the evidence of Dr. Belleau makes it clear that since slight changes of molecular structure can bring about marked changes in pharmacological activity, the extent to which pharmacological activities of a new substance having molecular features in common with substances known to have certain pharmacological activity are predictable is very narrow and it is much more difficult to make an accurate prediction of pharmacological activities than to make a prediction of chemical activity. On the whole, therefore, I am of the opinion that the evidence does not show that a negative answer to the Cripps question would be wrong. The defendant's objection on this ground accordingly fails.

The next objection taken to claim 8 was that it includes both the trans and the cis isomers of 2-phenyl-3-methylmorpholine and is invalid because the cis isomer is not a useful substance. In my opinion, the evidence on this point goes to the point of suggesting that because the two isomers are different, it would not be unreasonable to expect that their effects might be different. One might be useless or harmful while the other was useful and beneficial. Or one might be useful while the other was more useful. But this falls short of establishing that the cis isomer lacks utility or that it is harmful. The onus of establishing the objection by showing the lack of utility of the cis isomer was on the defendant and as the fact, if it is the fact, of its inutility has not been established, this objection also fails.

The third objection of this group was that claim 8 does not comply with s. 41(1) of the *Patent Act*. This subsection provides that:

> 41. (1) In the case of inventions relating to substances prepared or produced by chemical processes and intended for food or medicine, the specification shall not include claims for the substance itself, except

when prepared or produced by the methods or processes of manufacture particularly described and claimed or by their obvious chemical equivalents.

Claim 8, it will be recalled, refers to the process of claims 1, 2 or 3 or an obvious chemical equivalent, but as claims 2 and 3 are narrower process claims embraced within claim 1, for the purposes of considering the objection they can be disregarded. Claim 1, however, is a claim for a process for the production of the whole class of substances referred to in the specification. It does not specify the starting material to be used to produce 2-phenyl-3-methylmorpholine and so it was said claim 8, referring as it does to the process of claim 1, does not comply with s. 41(1).

In my opinion, this submission is well founded.

When s. 41(1) applies, and there is no dispute as to its application to the invention of 2-phenyl-3-methylmorpholine, it requires that the claim to such substance be limited to that substance when prepared or produced by the methods or processes which have been (*a*) particularly described, and (*b*) claimed, or (*c*) by the obvious chemical equivalents of the methods or processes which have been particularly described and claimed.

Here, the only limitation expressed in claim 8 is contained in the words "when produced by the process of claim 1, 2 or 3, or by an obvious chemical equivalent". And when one turns to claim 1 to see what process for preparing or producing 2-phenyl-3-methylmorpholine is therein claimed, one finds that it is not a claim for a process for the preparation of that substance but a claim for a process for the preparation of an enormous class of substances of which this substance is but one. In my view, claim 1 is not a claim for a process for the production of 2-phenyl-3-methylmorpholine even though that substance is one of the class, because it is clear that not all the members of the class of starting materials can be used to make 2-phenyl-3-methylmorpholine and claim 1 does not say that they can be used for that purpose, and at the same time, claim 1 does not say what starting material or materials may be used to make 2-phenyl-3-methylmorpholine. It thus does not state distinctly or in explicit terms any process for the production of that substance and we are back to the comment made earlier, that claim 1 as expressed

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does not fit the invention of 2-phenyl-3-methylmorpholine, but is a claim related solely to the alleged invention of the process for production of the class of substances. In *Winthrop Chemical Co. Inc. v. Commissioner of Patents*[1], the Supreme Court held that "a claim cannot be entertained for a substance falling within s-s. (1) of s. 41 unless a claim is also made in respect of the process by which it is produced", *vide* Martland J. in *Parke, Davis & Co. v. Fine Chemicals of Canada, Ltd.*[2]; "A process implies the application of a method to a material or materials", per Martland J. in *Commissioner of Patents v. Ciba Ltd.*[3]. In the same judgment, Martland J. quoted with approval the following from the judgment of Jenkins J. in *Re May & Baker Ltd. et al.*[4] at p. 295, line 17:

> . . . If I am right in the conclusions stated earlier in this judgment with regard to subject-matter, there is no inventive step, no element of discovery, merely in making new substances by known methods out of known materials.
>
> What is indispensably necessary in order to elevate a process of this description from a mere laboratory exercise to the status of a patentable invention is the presence of some previously undiscovered useful quality in the substances produced. Assuming that the substances produced do possess some previously undiscovered useful quality, for example some remarkable value as drugs, then although the methods are known and the materials are known yet the application of those methods to those materials to produce those new substances may amount to a true invention, because of the discovery that those particular known materials when combined by those methods not merely produce those new substances but produce, in the shape of those new substances, drugs of remarkable value.
>
> I think it necessarily follows that the identity of the materials chosen (by luck or good management) by the supposed inventor for the production of his new substances is of the essence of his invention.

Applying this to the invention of the process for the production of 2-phenyl-3-methylmorpholine, in my opinion it becomes plain that if there was anything "new and useful" within the meaning of s. 2(*d*) of the *Patent Act* about the process for the production of phenmetrazine capable of qualifying that process as an invention within the meaning of the definition, it was that by subjecting the particular known substance B-phenyl-α-methyl-B,B[1]-dihydroxy diethylamine to the morpholine ring closure by the known method of treating it with acid, a particular new and valuable drug could be produced. This, however, is not

[1] [1948] S.C.R. 46.
[2] [1959] S.C.R. 219 at 226.
[3] [1959] S.C.R. 378 at 383.
[4] 65 R.P.C. 255.

stated in claim 1 as the thing which the inventor regards as new and in which he claims an exclusive property for the identity of the starting material, which is of the essence of the invention of the process for the making of 2-phenyl-3-methylmorpholine, is not stated in the claim. It follows, in my opinion, that claim 1 cannot be regarded as a claim of the kind required by s. 41(1) as interpreted in the *Winthrop* case. The substance claim of claim 8 is therefore not limited, as it should be to comply with s. 41(1), to that substance when produced by a process for its preparation which is *claimed* and claim 8 is accordingly contrary to s. 41(1).

It was also urged in connection with the same submission that under s. 41(1) the claim for 2-phenyl-3-methylmorpholine must be limited not only to that substance when prepared by methods or processes which are *claimed* but also by methods or processes which have been *particularly described,* or their obvious chemical equivalents, and that the claim to that substance in claim 8 is not limited to the methods or processes which have been particularly described. This, in my opinion, raises a second fatal objection to the validity of claim 8. The only processes for the preparation of 2-phenyl-3-methylmorpholine which, in my opinion, can be said to be particularly described anywhere in the specification are those described in examples 2 and 9. Example 2 describes a process for production of 2-phenyl-3-methylmorpholine by dissolving B-phenyl-α-methyl-B,B^1-dihydroxydiethylamine-hydrochloride in concentrated sulphuric acid, allowing it to stand overnight at room temperature, then making alkaline and extracting. Example 9 describes a process by which the same diethanolamine hydrochloride is warmed with 10 per cent. hydrochloric acid for six hours on a water bath and the product then worked up "in the usual manner".

The claim to 2-phenyl-3-methylmorpholine in claim 8 is not stated to be limited to that substance when prepared or produced by these two processes or by their obvious chemical equivalents. It is not even stated to be limited to that substance when produced by the processes which were described generally, earlier in the specification or their obvious chemical equivalents, since the processes so described consist only in (*a*) introducing a diethanolamine

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of the class without heating into concentrated (96%) sulphuric acid; or (*b*) by treating it with diluted acid at a moderate temperature. Thus, even if contrary to my opinion, the general description of these processes could be regarded as sufficiently particular to meet the requirements of the expression "particularly described" in s. 41(1), and, if also contrary to my opinion, claim 1 does claim a process for the preparation or production of 2-phenyl-3-methylmorpholine, claim 8 would still not comply with the subsection.

To limit the substance claim of claim 8 only by reference to the substance when prepared by the process of claim 1, or an obvious chemical equivalent, is to ignore the requirement of s. 41(1) that the claim be limited as well to the substance "when prepared or produced by the methods or processes of manufacture particularly described . . . or by their obvious chemical equivalents". For, as previously pointed out, claim 1 is not limited as is the description to the use of concentrated sulphuric acid at room temperature and to the use of dilute acid at moderate temperatures, nor to the production of the morpholine ring closure by the action of acid on the diethanolamine. Nor do I think that whatever is embraced in claim 1 is necessarily embraced either within the processses described in the specification, or their obvious chemical equivalents. Claim 8 is thus broader than s. 41(1) permits and is accordingly invalid.

I should add that I have been somewhat puzzled as to whether or not these particular objections based on s. 41(1) were properly open to the defendant on the state of the pleadings, but a review of the argument satisfies me that the submissions were made without exception being taken by the plaintiff on that account and were answered by the plaintiff's counsel in the course of his reply. In these circumstances, I think the objection must be regarded as properly raised.

The last objection of this group was that claim 1 is invalid and that because of s. 41(1) claim 8 falls with it. The grounds on which claim 1 was said to be invalid comprise the third group of objections, but, of course, they are of interest in the present case only if the defendant is right in contending that the validity of claim 8 is dependent upon the validity of claim 1. Mr. Goldsmith's submission on this

point was that it follows from the *Winthrop* case[1] which held that a claim for a new substance in a patent to which s. 41(1) applies must be supported by a process claim, that the process claim which the statute requires must be one for a process for production of the particular substance claimed and that for this purpose a process claim must be judged as it stands and cannot be severed so that a part of it can be good while another part of it is bad.

Mr. Robinson's answer to this was that the only points resolved in the *Winthrop* case were that it was necessary, by reason of the language of s. 41(1) that the patent should contain a separate claim for the process and that the claim for the new substance should refer to that process claim rather than have the process set out as a portion of the substance claim. He went on to submit that even if claim 1 is invalid, that does not invalidate claim 8, that the process referred to in claim 8 is necessarily the process of claim 1 as applied to the manufacture of phenmetrazine and that the attacks on claim 1 related only to the process as applied to the manufacture of other compounds and were unrelated to the process as applied to the manufacture of phenmetrazine. He did not discuss the defendant's several objections to claim 1 but submitted that they do not arise.

To resolve this question, it seems to me to be necessary to start with s. 28(1) of the *Patent Act*. This subsection provides that subject to certain limitations set out in the section, any inventor of an invention may on presentation to the Commissioner of a petition setting forth the facts and on compliance with all other requirements of the Act obtain a patent granting to him an exclusive property in such invention. The right given by this subsection is given only to one who has in fact made an invention and the patent which he may lawfully obtain pursuant to the enactment is limited to one granting him an exclusive property in the invention which he has made. A patent granted for something which is not an invention at all is thus not obtained pursuant to the authority of the statute and is invalid. Similarly, where the inventor has made an invention, a patent purporting to give an exclusive property in more than the inventor has invented is also contrary to what the statute authorizes and subject to the saving effect of s. 60

[1] [1948] S.C.R. 46.

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may also be invalid. These are fundamental statutory limits on the validity of patents which may lawfully be obtained. But in addition to these limitations, the statute also imposes certain requirements on one who seeks to obtain a patent for an invention which he has made, and by the terms of s. 28(1) he is entitled to obtain a patent giving him an exclusive property in "such invention" only on compliance with these requirements. Requirements of this nature are found in ss. 35, 36(1), 36(2) and 41(1). By s. 35 the applicant is required to send in with his application for a patent a specification of the invention. Section 36(1) then prescribes what the specification must contain by way of description and explanation of the invention and s. 36(2) requires that

> The specification shall end with a claim or claims stating distinctly and in explicit terms the things or combinations that the applicant regards as new and in which he claims an exclusive property or privilege.

The claims made pursuant to this requirement become the definition or measure of the invention in which an exclusive property is granted by the patent, for by s. 46 it is provided that every patent granted under the Act shall contain the name of the invention, with a reference to the specification, and shall grant to the patentee . . . the exclusive right, privilege and liberty of making, constructing and vending to others to be used *the said invention,* i.e., the invention of which the name is stated with a reference to the specification which in turn, as required by s. 36(2), must state in the claims what the inventor regards as new and in which he claims an exclusive property. That this is the effect of the claims is also supported by the opinion of Lord Russell of Killowen in *Electric and Music Industries v. Lissen Ltd.*[1], expressed at p. 41 as follows:

> A claim is a portion of the specification which fulfills a separate and distinct function. It, and it alone, defines the monopoly.

and by the opinion of Rinfret J. (as he then was) in *Smith Incubator Co. v. Seiling*[2], where he said at p. 259:

> In our view the rule is that the claims must be regarded as definitely determining the scope of the monopoly having regard to the due and proper construction of the expressions they contain.

[1] (1938) 56 R.P.C. 23. [2] [1937] S.C.R. 251.

It follows from the foregoing that a patent which includes in its specification a claim which claims more than the inventor has invented purports to grant an exclusive property in more than the inventor has invented and at least in so far as that claim is concerned the patent, in my opinion, is not granted under the authority of the statute and is therefore not lawfully obtained. I think it also follows (even allowing for full scope for the operation of s. 60) that no rights whatever can accrue to the patentee from the presence in the specification of such a claim, either for the purpose of enforcing the property rights thereby purported to be granted or for the purpose of fulfilling a statutory requirement such as that in s. 41(1) that a claim for a new substance in a patent to which that substance applies be limited to the substance when produced by a process which has been "claimed". For as I view it, a claim which is invalid because it claims more than the inventor invented is an outlaw and its existence as defining the grant of a property right is not to be recognized as having any validity or effect. Nor is there in the statute any provision for separating what may be good in such a claim, in the sense of what is in accordance with the statute, from what is bad in it, in the sense of what is contrary to or unauthorized by the statute.

Nor do I think the effect of the judgment in the *Winthrop* case is so limited as Mr. Robinson submits. The case holds that in a case to which s. 41(1) applies, a claim for a new substance must be accompanied by a claim for a process for producing it, but it is, I think, impossible to read the judgment as meaning that a claim for an exclusive property to which the inventor was not entitled and which was therefore illegal and invalid could serve the purpose.

Estey J., speaking for himself and Rinfret C.J., discussed the interpretation of the subsection thus at p. 48.

> The language of section 40(1) construed according to the grammatical and ordinary sense in which the words are used indicates that a patent for the substance separate and apart from the method or process by which it was produced could not be granted unless the word "claimed" is construed to have a meaning such as that suggested by the respondent.
>
> Sections 34 and 35 under the heading "Specifications and Claims" set forth the requisites which an applicant must include in his specification. In the main there are two parts to the specification under these sections. That under section 35(1) may be referred to as the description

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and that under section 35(2) the claim. The description portion discloses the invention and its operation and use and such details as required in 35(1). Section 35(2) provides:

> "The specification shall end with a claim or claims stating distinctly and in explicit terms the things * * * in which he claims an exclusive property or privilege."

These sections 34 and 35 provide for and indicate the reason, purpose and meaning of both the description and the claim portions of the specification. The claim sets forth precisely the subject and the limits of the "exclusive property or privilege" or the protection desired in the patent. These provisions indicate the meaning and purpose of the claim, and the word so used and understood cannot mean merely as "defined in the claim so as to be made a constituent element of the claim" as the respondent submits.

In section 37(2) the phrase "describes and claims" appears, and again these words are used in the same sense as in section 35 and their separate significance is again apparent.

There appears no reason to conclude other than that Parliament intended that these words "claims" and "described and claimed" should have the same meaning and significance in section 40(1). So construed it appears that when Parliament adopted in section 40(1) the words

> "the specification shall not include claims for the substance itself, except when prepared or produced by the methods or processes of manufacture particularly described and claimed,"

it meant that the applicant's specification should describe the method or process and claim a patent therefor in the manner specified in section 35. Under this section 40(1) therefore a claim for "an exclusive property or privilege" with regard to the method or process by which the substance is produced may be accompanied by a claim for a patent with respect to that substance but a claim for a patent with respect to the substance alone cannot be entertained.

In this reasoning, the validity of the required claim for the process seems to me to be an underlying assumption and I think the same applies to the following passage from the judgment of Rand J. at p. 55:

> Considering then the language of Section 40 ss. (1), I think it quite impossible to say that it has not a plain and ordinary meaning which is quite consistent with the remaining provisions of the Act and is wholly without incongruity or absurdity. It is in these words:
>
> "40. (1) In the case of inventions relating to substances prepared or produced by chemical processes and intended for food or medicine, the specification shall not include claims for the substance itself, except when prepared or produced by the methods or processes of manufacture particularly described and claimed or by their obvious chemical equivalents."
>
> I observe, first, as Mr. Robinson conceded, that the primary meaning of the word "claim" or "claimed" in the statute is the specific assertion of invention for which a patent is sought by the application. Then there is the word "include" in the fourth line, the sense of which is said to be that of "contain", but which in the first instance at least, I feel bound to take, in the particular context, as implying that the claim for the substance is one of a plurality of claims including that for the method

or process. So reading these words, the subsection clearly denies any right to a patent for a substance unless there is, in addition, a claim in its technical sense for the mode or process of producing it.

I am accordingly of the opinion that if claim 1 is invalid, it cannot serve to fill the requirement of s. 41(1) that a claim for a new substance in a patent to which that subsection applies be accompanied by a claim for the process of producing the substance and be limited to the substance when produced by that process or an obvious chemical equivalent. In this view, the defendant's objections to claim 1 are relevant to the issue of the validity of claim 8.

These objections make up the third group to which I have already referred. In this group there were eight objections raised, but in view of the conclusion which I have reached on one of them, it is unnecessary for me to deal with the others and undesirable as well that I should do so since no argument was presented by Mr. Robinson in reply to them. The particular objection with which I shall deal was that claim 1 is for a known process for the production of an almost infinite number of end products of which only one has been described from the point of view of pharmacology and the remainder are not useful and so the process as claimed lacks utility.

As previously mentioned, the specification expressly states that substituted morpholines of the defined class produced according to the invention are valuable pharmaceuticals or intermediate products for the production of pharmaceuticals and that the other compounds of the class will produce effects similar to those which have been described as the effects of 2-phenyl-3-methylmorpholine. This, together with the presence in the specification of the eight examples of methods of producing substances of the class other than 2-phenyl-3-methylmorpholine, leads me to conclude that as a matter of construction the specification claims the described methods whenever applied to the production of any of the morpholines which fall or would fall within the scope of claim 1 whether they are useful as stated or not. In *Ciba Ltd. v. Commissioner of Patents*[1], the reasoning of Jenkins J. in *Re May & Baker Ltd. et al.* was applied to the consideration of whether or not process claims consisting of the application of known methods to

[1] [1959] S.C.R. 378.

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known materials to produce new and useful products disclosed an invention patentable under the Canadian statute, and Martland J. in delivering the judgment of the Supreme Court, after quoting from the judgment of Jenkins J., said at p. 383:

> In my view the reasoning is sound and should be applied in the present case. To constitute an invention within the definition in our Act the process must be new and useful. *There is no question as to the process here being useful, as it produces compounds which have been admitted to be both new and useful.*
>
> Is it a new process? Is the element of novelty precluded because it consists of a standard, classical reaction used to react known compounds? In my opinion the process in question here is novel because the conception of reacting those particular compounds to achieve a useful product was new. A process implies the application of a method to a material or materials. The method may be known and the materials may be known, but the idea of making the application of the one to the other to produce a new and useful compound may be new, and in this case I think it was.

A part of the passage which Martland J. quoted from the judgment of Jenkins J. was that already referred to and quoted in (*ante* p. 236) these reasons.

From what Martland J. and Jenkins J. said in the passages quoted, it appears that the utility of the processes in a case of this kind depends on the utility of the products produced by such processes and it would seem to follow that a claim for processes which produce products which are not useful in the patent sense lacks utility and is therefore invalid. Nor will the fact that some of the processes so claimed will produce useful products save the claim; *vide* Jenkins J.[1] at page 288, lines 5 to 11.

Now while the burden of proving that the process claimed in claim 1, as therein defined, would not produce a whole class of useful substances rested on the defendant, I think I should observe that the proposition that all of the myriad of substances which could be produced by the process of claim 1 have effects similar to those of phenmetrazine (which is the only utility described or disclosed), when it is apparent from the mere size of the class that most of its members could never have been made or tested, is so exorbitant as to require little in the way of evidence to dispel any presumption of its truth. But however that may be, it is clearly established by the evidence of Dr. Belleau that the pharmacological effects of new substances

[1] 65 R.P.C. 255.

are not predictable except within very narrow limits and lengthy testing of new substances on animals as well as humans is necessary to determine what the effects will be. There is also evidence that the number of known organic compounds does not exceed three millions which, when compared with the number of conceivable substances comprised within the class defined in claim 1 calculated as being far in excess of four billions, satisfies me that the great bulk of these substances have not in fact been produced or tested and that nothing is in fact known of what their pharmacological effects may be. Nine substances out of this enormous number are indeed mentioned in the examples, one of the nine being phenmetrazine, but Dr. Belleau knew of no pharmacological use for any of them except phenmetrazine, or for any of the others not included in the nine examples. Had there been any known pharmacological use for any of these products, I think Dr. Belleau would have known and been able to tell about it, and his inability to do so satisfies me that no such use is known. On balance, therefore, I think it improbable that all or the majority or even a substantial number of the members of this class have the utility referred to in the specification, and in my opinion claim 1 is accordingly invalid and because it is invalid, claim 8 is invalid as well.

In view of the conclusion which I have reached as to the validity of claim 8, it is not strictly necessary that I should deal with the question of infringement, but as this question was argued at length and is largely one of fact, I shall express my view on it as briefly as I can in case it may be of some importance in the event of an appeal. There are two aspects to this question, the product aspect and the process aspect and for the purpose of considering the question I shall assume that claim 8 is valid. I turn first to the product aspect. What is complained of is that the defendant sold phenmetrazine hydrochloride which is within the scope of the patent. I have already indicated that in my opinion as a matter of construction the expression "2-phenyl-3-methylmorpholine" in claim 8 refers to the base and not to any of the salts, which are in fact different substances from the base. The sale complained of will therefore be an infringement of claim 8 only if phenmetrazine hydrochloride is an equivalent of phenmetrazine itself. The question of equivalents was discussed at length in the judgment of the

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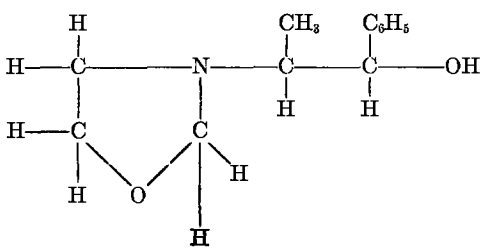
President of this Court in *McPhar Engineering Co. of Canada, Ltd. v. Sharp Instruments Ltd. et al.*[1], and having regard to the principles therein referred to, I think it is clear that for the purpose of obtaining the pharmacological results which may be obtained by oral administration, phenmetrazine hydrochloride is an equivalent of phenmetrazine itself for, as soon as it reaches the stomach, the phenmetrazine base is immediately converted to phenmetrazine hydrochloride and from that point onward the action is precisely the same whether the base or the hydrochloride has been taken. The same function can thus be achieved by taking either, the conversion of the base into the hydrochloride in the stomach being a completely immaterial feature of the use of the substance. When either substance has been taken the phenmetrazine hydrochloride salt is considered to be present in the gastric fluid as dissociated phenmetrazine cations and chloride anions. As these proceed through the intestine, some of the phenmetrazine cations are rendered basic again by the alkaline intestinal fluids and what ultimately reaches the body cells where the effects are produced are both the basic and the protonated forms. It is not known whether the effects are due to the basic or the protonated form or to both, but the forms which reach the cells and produce the results are the same whether the salt or the base has been taken. In the invention of phenmetrazine an essential feature, in my opinion, lay in the development of the substance by that name which when introduced into the stomach would operate to supply to the body cells the basic or protonated form of phenmetrazine capable of producing the desired effects without at the same time introducing into the body system anions that are not usually present or that it is otherwise undesirable to introduce. To fulfill this function by introducing into the stomach a hydrochloride salt of the substance instead of the base is to make use of this feature of the invention by a means which differs only in an immaterial and non-essential way. It involved no exercise of any ingenuity for a pharmacologist to realize that the hydrochloride salt of phenmetrazine would be equally convenient to administer for the purpose since he would have known that the phenmetrazine itself would be converted to that salt immediately on entering the stomach, and the method of preparing that salt from the base is a routine

[1] 21 Fox P.C. 1 at 55 *et seq.*

chemical procedure and is referred to in the specification. I am therefore of the opinion that the sale of phenmetrazine hydrochloride does in fact infringe claim 8 provided, of course, that it has been made by one of the processes therein mentioned.

This brings me to the second, or process, aspect of the question and in this connection a brief explanation of some further facts will be necessary.

The phenmetrazine hydrochloride sold by the defendant was made in Italy by Industria Chimica Profarmaco S.p.A. by a process developed by the chemical research staff of that company under Professor Rossi. The staff first sought and after a time found a cheaper and easier way to produce B-phenyl-α-methyl B,B1-dihydroxy-diethylamine for use as starting material for the production of phenmetrazine, but in this method the diethanolamine was produced in water solution from which it was difficult and impractical to extract it. After some months of experiment, in an effort to find a commercially satisfactory way to extract the diethanolamine, it was found that by adding formaldehyde (C H_2O) to the reaction mixture, an oily liquid separated out and could be removed and purified without difficulty. The oily liquid was identified as an oxazoladine with a structural formula which may be represented as follows for comparison with that of B-phenyl-α-methyl-B,B1-dihydroxy-diethylamine:



This was a new substance not previously known in chemistry. It was subsequently found that treatment of this substance with a 50 per cent. aqueous solution of sulphuric acid at 115° C in a pilot plant produced a 70 per cent. yield of phenmetrazine, but this was not a satisfactory process because in the process formaldehyde was formed as a by-product and it had a tendency to react with the morpholine. After several test runs of the process in the pilot plant,

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urea was added to the starting materials in the hope of improving the yield of phenmetrazine by eliminating the formaldehyde as it formed. Urea was known to react with formaldehyde to form insoluble substances and the urea was added in the hope that such substances would be formed and would separate out. It was found that by adding urea to the reaction mixture the yield of phenmetrazine in the pilot plant was raised to 85 per cent. and it was by this process that the material sold by the defendant was produced. In this process, though the starting material is treated "in the presence of acid", the starting material itself is not a diethanolamine at all and on first impression it appears to be a widely different process from that referred to in claim 1. On the evidence, however, the matter is not so simple and it becomes necessary to look closely both at claim 1 to see what it embraces and at the Profarmaco process as well to see what happens in it.

Claim 1 refers to a process for the production of a class of substituted morpholines characterized in that diethanolamines of a certain class are treated in the presence of acid. As a matter of construction the claim in my opinion refers only to the treatment in the presence of acid of diethanolamine bases of the defined class for the structural formula given is only that of the bases, but because any chemist would observe at a glance that the treatment of such a diethanolamine in the presence of acid would involve initially the formation of the diethanolamine salt of that acid, I think that the treatment of such a diethanolamine salt in the presence of acid to form a substituted morpholine of the class would be a chemical equivalent of the process as defined and anyone who made such a substance in that way would have taken the essential feature of the process of claim 1 notwithstanding the omission of the immaterial initial step of the process of the claim in which the base is converted to the salt of the acid. The class of diethanolamine bases so defined includes B-phenyl-α-methyl-B,B^1-dihydroxy-diethylamine which in this discussion I shall refer to as "the diethanolamine". Now as I understand the evidence, the first stage of what occurs in the Profarmaco process is the formation of the oxazoladine salt of the sulphuric acid and the reaction then proceeds by way of the treatment of that salt in the presence of the acid and urea, the function of the urea being as already

mentioned to remove formaldehyde from the reaction mixture as it forms. The question then arises whether the reaction proceeds directly to the formation of the phenmetrazine salt from the oxazoladine salt by way of an opening of the oxazoladine ring at the bond between the oxygen atom and the carbon atom in B position from the nitrogen, and immediate formation of a linkage between that carbon atom and the oxygen atom shown on the right hand end of the structural formula or proceeds by way of hydrolysis of the oxazoladine to form a sulphate salt of the diethanolamine and formaldehyde and then to ring closure to form the phenmetrazine salt. If the latter is the correct view, the Profarmaco process involves as one of its steps or stages the treatment of the diethanolamine salt in the presence of the acid. On this question, the opinions of the experts were not in agreement. Dr. Wright was of the opinion that the reaction proceeded directly to the morpholine ring closure, while Dr. Belleau was equally firm in taking the other view. Professor Rossi on the other hand took the view that it is impossible to tell what course the reaction takes. To one so unlearned as I am in the niceties of chemical reactions, the view of Professor Rossi has its attractions, but on the evidence as a whole, I think I must resist the temptation to adopt it. All three experts agreed with a statement in a textbook on heterocyclic compounds edited by Robert C. Elderfield that "Hydrolysis of oxazolodines to a carbonyl compound and an ethanolamine can *usually* be effected by water alone and appears to be catalyzed by both acids and alkali hydroxides." With this may be taken the fact established in an experiment carried out by Dr. Wright that the diethanolamine is present in a pure state in a mixture of the oxazoladine and 50 per cent. sulphuric acid which has been allowed to stand at room temperature for 72 hours. This indicates that, under these conditions, the oxazoladine is hydrolized to form a sulphuric acid salt of the diethanolamine. In the opinion of Dr. Belleau, the conditions of the Profarmaco process, i.e., 50 per cent. aqueous solution of sulphuric acid and a temperature of 115°, are vigorous hydrolizing conditions and since hydrolysis of this oxazoladine to form the diethanolamine has been shown to occur at room temperature, I can see in the evidence no sufficient reason to think that it would not also occur to some extent in the course of raising

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the temperature from room temperature to 115°C. Nor is there anything but theory, on which opinions are not in agreement, to the contrary. To my mind, neither Dr. Wright's experiment with the oxazoladine in concentrated sulphuric acid at room temperature in which after 60 hours phenmetrazine had formed, nor his subsequent experiments in hydrolizing the oxazoladine in aqueous solutions of ammonia, establish either that hydrolysis does not occur in the earlier of these experiments prior to the formation of phenmetrazine or that hydrolysis does not occur as a first step in the Profarmaco process. And whether or not either of Dr. Belleau's experiments can be regarded as paralleling the Profarmaco process closely enough to afford any support for the view that hydrolysis does occur, there is no indication from them that it does not occur. On the whole, therefore, and particularly having regard to the hydrolysis which occurred in Dr. Wright's experiment with the oxazoladine in 50 per cent. sulphuric acid at room temperature and to the fact that heating such a mixture to 115° would probably enhance and accelerate the hydrolizing process, I think that the balance of probabilities favours the view that hydrolysis of the oxazoladine to form the diethanolamine does in fact occur as a stage of the reaction of the Profarmaco process. Moreover, while there are theoretical possibilities of some of the oxazoladine molecules following a different course or courses or being involved in a different reaction or reactions to form phenmetrazine, in the view I take, there is no sufficient evidence to establish that any do in fact follow such other courses or that such reactions do in fact occur.

In this view, while the process of claim 1 as I have construed it is not involved in the Profarmaco process because at no stage is a diethanolamine base of the class set out in claim 1 involved, the Profarmaco process does involve a stage which is equivalent to the process of claim 1 in that it involves the production of phenmetrazine by the treatment in the presence of sulphuric acid of a sulphate salt of a diethanolamine of the class referred to in claim 1. The final question then arises whether the Profarmaco process was an obvious chemical equivalent of the process of claim 1 within the meaning of s.41(1).

In discussing a somewhat similar situation in *Actiengesellschaft fur anilin Fabrikation in Berlin v. Levinstein Ld.*[1], Warrington L.J., speaking for the Court of Appeal, said at p. 292:

> The difference really insisted on by the Defendants is in the process, not in the product. Shortly stated, it is that, whereas the Plaintiffs prescribe and claim the use of dinitrophenol, an acid substance, as the material to be operated upon, the Defendants use sodium dinitrophenolate, the corresponding sodium salt. The Plaintiffs contend that this is, in substance, no variation, or a merely colourable variation, of their process; whether they are right in this contention is the question for decision.

Then after discussing the facts, he proceeded at p. 293 as follows:

> On the whole, after following carefully the passages from the evidence which were read to us and the comments of Counsel thereon, we have come to the following conclusions: First, the Specification is in terms confined to a process of boiling, with the solution indicated, dinitrophenol, a definite chemical combination of which the formula is given; secondly, the dinitrophenolate of sodium is another and a different chemical combination having physical properties distinct from those possessed by dinitrophenol; thirdly, that a process of boiling sodium dinitrophenolate with the solution mentioned in the Plaintiffs' Specification would not be covered by the Claim, unless the Plaintiffs could show that it was part of the common knowledge at the date of the Patent, not only that, as a matter of chemical theory, the sodium dinitrophenolate would be formed in the course of the reaction, but that, in the practical application of the process on a commercial scale, the same result would be obtained by starting with the sodium dinitrophenolate as with the dinitrophenol; fourthly, that the Plaintiffs have not established that there was, at the date of the Patent, the necessary common knowledge, and that, therefore, the Defendants' process is not within the Claim and the charge of infringement fails. We come the more readily to the conclusion that the Plaintiffs and their advisers did not know that it was possible to obtain their dye by the substitution of the sodium dinitrophenolate for dinitrophenol, because, if they did know it, it is difficult to understand why such possibility was not pointed out in the Specification. We think it is clear on the evidence that, for commercial purposes, the substitution in question was economically an advantage, and, accordingly, by omitting to mention it, they were, on the assumption that they knew the facts, laying the Patent open to attack on the ground that the Patentees had not informed the public of the best way known to them of putting the invention in practice.

On the facts of the present case, the presumption of s. 41(2), if it arises at all, which I doubt in view of the fact that phenmetrazine hydrochloride is not the substance referred to in claim 8, is displaced by the evidence of Professor Rossi that the material sold by the defendant was produced by a process in which an oxazoladine not

[1](1921) 38 R.P.C. 277.

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known at the time of the invention of the patent, rather than a diethanolamine of the class defined in claim 1 was treated in the presence of acid and to support the charge of infringement it would, in my opinion, be necessary for me to conclude not merely that in the reaction conditions the oxazoladine would be first hydrolyzed to form a diethanolamine of the class defined in claim 1 and a carbonyl compound but as well that it was within the common knowledge that this would occur. In my opinion, it would also be necessary to find that it was within the common knowledge that in the practical application of the process on a commercial scale, phenmetrazine could be obtained by starting with this oxazoladine as with the diethanolamine.

The evidence, however, in my view, indicates that it was not within the common knowledge that this particular previously unknown oxazoladine would hydrolyze to form a sulphate salt of the diethanolamine under the conditions of the Profarmaco process. If anyone had thought of such an oxazoladine it might well have been a fair prediction on the basis of what was then known of oxazoladines in general that this one would behave as the others and that hydrolysis would probably occur, but while I have reached the conclusion on what I regard as a preponderance of evidence—which includes evidence of recent experiments—that the probabilities are that hydrolysis does occur and that the Profarmaco reaction in fact follows that course, that such is the course of the reaction is not accepted as fact by either Professor Rossi or Dr. Wright, both of whom are exceedingly learned men in the chemical field, and it seems to me that when a point of this kind which depends to so great an extent on theories and inferences which may ultimately turn out on further examination to be erroneous, a conclusion reached as mine has been reached can hardly be characterized as one that was within the common knowledge of a substance which up to the material time had never been made or even thought of. I therefore think even assuming, as I have found, that the Profarmaco process involves a stage which is the chemical equivalent of the process of claim 1, that it was not an obvious chemical equivalent of that process within the meaning of s. 41(1) of the Act.

Moreover, with respect to what I think is the more important fact necessary to support the claim of infringement, the evidence in my view clearly shows that it was not within the common knowledge that in the practical application of the process on a commercial scale phenmetrazine would be obtained by starting with the oxazoladine as with the diethanolamine, for it took Professor Rossi and his staff some months of experiment and research before they discovered the oxazoladine and that phenmetrazine could be made in this way and even when this had been discovered, it took some time to devise by the addition of urea a way to make this method of producing phenmetrazine give a yield which would be satisfactory for the purpose of commercial production of the substance. The Profarmaco process as described by Professor Rossi appears to afford substantial practical advantages over the use of the diethanolamine as starting material and if, indeed, it was known that phenmetrazine could be made by starting with the oxazoladine one may wonder that the patentee did not think of it and disclose it in his specification. After such a discovery has been made, it may well appear to some to be more or less obvious, but I think the obviousness or otherwise of it must be judged in the light of what was known at the material time and of what was entailed in making the further discovery without regard to how it may appear after the further discovery has been made. I may add that for the purposes of the present case, I think it is immaterial whether the appropriate time is the date of the invention of the patent or the date when the later discovery was made for my opinion would be the same in either case. I am accordingly of the opinion that the Profarmaco process is not an obvious chemical equivalent of the process of claim 1 within the meaning of s. 41(1), and as I have also already expressed the view that the Profarmaco process is not within the scope of claim 1 as I have construed it, it follows that the claim of infringement fails.

Accordingly there will be judgment for the defendant dismissing the action with costs.

Judgment accordingly.

1961
May 24
1962
Mar. 2

BETWEEN:

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

AND

VICTOR TRUDEAU .....RESPONDENT.

Revenue—Income tax—Classification of properties—Recapture of capital cost allowance—Income Tax Act, R.S.C. 1952, c. 148, ss. 11(1)(a), 20(1)—Income Tax Regulations, s. 1101(1).

The respondent in partnership with another carried on a room rental business at two different places under the respective registered firm names of Alpine Rooms Reg'd. and New Frontenac Hotel and Tavern. On the sale of the Alpine property the Minister ruled that the respondent had been carrying on two separate businesses and pursuant to s. 20(1) of the *Income Tax Act* and s. 1101(1) of the *Income Tax Regulations* added to the respondent's declared income an amount to recapture the capital cost allowance. The respondent appealed to the Tax Appeal Board on the ground that he was carrying on but one business at the two places and the recapture of capital cost allowance should be deferred until sale of the entire business. On an appeal from the Board's decision allowing the respondent's appeal to it

Held: That Alpine Rooms Reg'd. and New Frontenac Hotel and Tavern constituted two different businesses could be inferred from the fact that each was a legal entity operating under its own firm name. A judgment creditor of the one could have no claim on the assets of the other. Their fiscal years differed, as did the characteristics in the operation of a rooming house as distinguished from that of a hotel and tavern.

2. That the appeal should be allowed and the Minister's ruling affirmed.

APPEAL from a decision of the Tax Appeal Board[1].

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

Paul Boivin, Q.C. for appellant.

Jacques Valade for respondent.

DUMOULIN J. now (March 2, 1962) delivered the following judgment:

Le Ministre du Revenu national interjette appel d'une décision de la Commission d'appel de l'Impôt, datée le 22 avril 1960[1], annulant une nouvelle cotisation, émise le 16 septembre 1958, qui ajoutait un montant de $7,277.58 au revenu de l'intimé pour l'année d'imposition 1957.

[1] (1960) 24 Tax A.B.C. 423; 60 D.T.C. 430.

Les parties déposèrent au dossier de l'instance la transcription des témoignages entendus par la Commission d'appel, en sorte que les procureurs traitèrent uniquement des questions de droit.

L'intimé, Victor Trudeau, domicilié à Longueuil, près Montréal, poursuit de multiples occupations, celles de: courtier en assurances, tavernier, commerce de location de chambres et courtier en immeubles (preuve, p. 4).

En ce qui regarde le commerce de location de chambres, Trudeau l'exerçait à Montréal, à parts indivises avec un certain René Daoust, sous les raisons sociales enregistrées de «Alpine Rooms Reg'd», au numéro 2015, avenue McGill College, puis encore sous celle de «New Frontenac Hotel and Tavern», à 2553 est, rue Rachel.

L'entreprise de Alpine Rooms Reg'd fut vendue dans le cours de 1957 et le ministère du Revenu national, selon les dispositions des articles 11(1)(*a*) et 20(1) de la Loi de l'Impôt (S.R.C. c. 148), et de l'article 1101 des Règlements, inclut dans le revenu de l'intimé, pour telle année, une somme additionnelle de $7,277.58, à titre de dépréciation récupérée.

L'appelant soutient que les deux sociétés commerciales précitées constitueraient des «catégories distinctes» d'entreprises, partant, susceptibles de taxation distincte.

Trudeau, l'intimé, s'est inscrit en faux contre cette cotisation supplémentaire prétextant:

> 4. Que l'intimé était propriétaire indivis de la moitié des biens dépréciables d'une même catégorie.
>
> 5. Ces biens de même catégorie étaient, pour l'intimé, partie d'une entreprise exploitée à deux endroits, soit l'Alpine Rooms Reg'd et le New Frontenac Hotel and Tavern . . . (Voir réponse à l'avis d'appel).

Il s'agit donc uniquement de décider si la maison de chambres Alpine Rooms Reg'd et les chambres en location au numéro civique 2553 est, rue Rachel, connues sous l'appellation sociale de New Frontenac Hotel and Tavern forment une seule et même entreprise ou, au contraire, deux entreprises différentes.

Au cours de son témoignage devant la Commission d'appel, Trudeau déclara qu'il n'y avait pas de salle à manger dans l'immeuble Alpine Rooms et que le seul commerce auquel on se livrait à cet endroit était celui de location de chambres. Par contre, il précise que (preuve p. 7)

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«l'édifice du New Frontenac consiste en une taverne au rez-de-chaussée; un restaurant au rez-de-chaussée occupé par un locataire, et puis, à l'étage supérieur, il y a trente chambres».

Ce même témoin dira encore que le personnel, ou selon son expression, «le staff», affecté à la taverne du New Frontenac, différait de celui préposé à l'entretien des trente chambres.

Trudeau, pour des fins de convenance pratique, avait cru devoir former deux sociétés légalement différentes l'une de l'autre, sous les vocables précités. A mon avis, il semblerait étrange que tel commerce, exploité sous plusieurs raisons sociales distinctes, demeurât, vis-à-vis la loi fiscale, toujours et partout, une seule et même «entreprise». La distinction à établir porte moins sur la nature même du commerce que sur l'entité légale des entreprises. Si donc nous devons conclure, en toute logique, que Alpine Rooms Reg'd est une entreprise de négoce, et New Frontenac Hotel and Tavern une autre, il importe peu que l'exploitation concerne des biens de même catégorie. Telle est, du reste, par voie d'analogie, la disposition du Code de procédure civil qui, au dernier paragraphe de l'article 122, énonce que:

> tant qu'une société commerciale enregistrée n'est pas dissoute, elle peut être poursuivie sous sa raison sociale, mais le jugement n'est exécutoire que contre ses biens.

Conséquemment un créancier de la maison de chambres Alpine Rooms serait empêché de parfaire l'exécution du jugement obtenu contre celle-ci sur les biens de New Frontenac Hotel, en alléguant qu'on y fait un même commerce et que Trudeau est co-propriétaire aux deux endroits.

Le procureur de l'intimé prétend que le recouvrement de la dépréciation afférente à la disposition des biens du commerce vendu devrait être différé jusqu'au jour de la vente de l'hôtel New Frontenac. C'est aller, je crois, beaucoup au delà de l'intention manifeste de la loi et du sens commun.

Il convient de reproduire quelques extraits du témoignage de Trudeau, quant à l'administration du New Frontenac Hotel and Tavern. Le témoin, interrogé par son procureur, Me Walter Guillery, répond ainsi aux questions:

> Q. Est-ce que vous pourriez nous dire, monsieur Trudeau, quelle est la différence entre un hôtel, réellement, et une maison de chambres?

R. Un hôtel, nous avons le nom de New Frontenac Hotel relativement à ce qu'on doit tenir, c'est-à-dire une salle à manger. On n'a jamais tenu de salle à manger. Et, par conséquent, on a toujours eu la licence provinciale sous le nom d'hôtel et c'est toujours resté comme ça. Et puis, le gouvernement ne nous a jamais demandé de changer, mais c'est exactement les chambres seulement. On peut garder une pièce où on peut mettre une table avec une nappe pour montrer qu'il y a une salle à dîner, mais on ne sert pas de repas.

Q. Maintenant, la taverne, est-ce que c'est le même personnel, le même «staff» qui travaille à la taverne et à la maison de chambres?

R. Non. Il y a un «staff» pour la taverne et un «staff» pour la maison de chambres.

Q. Est-ce que vous opérez la taverne indépendamment?

R. Oui, indépendamment, complètement.

Cette dernière assertion est contredite, nous le voyons, à la page 14 de la transcription des témoignages, où Trudeau, auquel on exhibe le bilan du New Frontenac Hotel and Tavern pour 1957, doit reconnaître que le revenu provenant des locations de chambres, dans cet immeuble, se confond avec la somme globale des recettes dont la grosse partie provient de l'exploitation de la taverne. Joignons aussi que la déclaration de société dans le cas de Alpine Rooms Reg'd prévoit l'exploitation d'un commerce de chambres, alors que dans le cas du New Frontenac Hotel, cette attestation statutaire fait mention de l'exploitation d'une hôtellerie. Enfin, l'exercice financier annuel de Alpine Rooms Reg'd se clôturait le 30 novembre et celui du New Frontenac Hotel, le 31 décembre. Chacun de ces indices, dont aucun n'est décisif en soi, semble indiquer, dans cette question de fait, que l'intimé exploitait deux entreprises distinctes.

L'article 1101, paragraphe 1 des règlements de l'Impôt sur le revenu se lit de la façon suivante:

1101(1) Lorsque l'Annexe B des présents Règlements comporte la description de plus d'un des biens d'un contribuable, sous la même catégorie, et

(*a*) qu'un des biens a été acquis aux fins de gagner ou de produire le revenu d'une entreprise, et

(*b*) qu'un des biens a été acquis aux fins de gagner ou de produire le revenu d'une autre entreprise ou des biens,

une catégorie distincte est par les présentes prescrite pour les biens qui

(i) ont été acquis aux fins de gagner ou de produire le revenu de chaque entreprise, et

(ii) seraient par ailleurs compris dans la catégorie de l'Annexe B des présents Règlements.

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Or, ici le commerce de chambres à l'Alpine Rooms Reg'd et l'exploitation d'une hôtellerie avec taverne adjointe au New Frontenac Hotel offrent, je le crois, les caractéristiques d'exploitations différentes telles que prévues par la loi fiscale et le règlement 1101(1).

Pour les motifs qui précèdent, je suis d'avis d'accueillir l'appel et de déclarer conforme à la loi l'inclusion d'une dépréciation récupérée au montant de $7,277.58 dans le calcul du revenu de l'intimé, Victor L. Trudeau, pour l'année d'imposition 1957.

L'appelant aura droit de recouvrer les dépens encourus après leur taxation.

Jugement conforme.

1960

Sept. 29, 30

1962

May 8

BETWEEN:

CADILLAC CONTRACTING AND DEVELOPMENTS (TORONTO) LIMITED ..... APPELLANT;

AND

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

Revenue—Income—Income tax—Land purchased in part for investment purposes later sold en bloc—Whether profit on part purchased for investment subject to tax—The Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e).

The appellant company was incorporated in September 1953 with objects which included dealing in land and holding land for investment purposes. In May 1954 it acquired title to fifty acres of land in North York Township which the syndicate of persons at whose instance the appellant was incorporated had agreed to buy in April 1953 for $250,000. The intention of the syndicate when purchasing the property was to erect apartment buildings on 35 acres of the land to be held as an investment and subdivide the remainder for single family dwelling lots. Difficulties were encountered in carrying out these plans because of the absence of water and sewer facilities and some time after the appellant company acquired title to the property it was decided to subdivide and sell as single family dwelling lots all but ten acres of land, later reduced to five acres, which was reserved by the appellant for the apartment house project.

In December the Township advised the appellant's plan of subdivision would be recommended for approval provided the appellant conveyed 11 lots to the Township and entered into a contract with it for the construction of roads and sewers, the installation of services and the payment of taxes. In February 1955 the appellant proceeded through real estate agents to sell all the lots in the proposed subdivision other than those required by the Township and those it had reserved for the apartment project. Most of the agreements provided that the sale would be null and void if the plan was not registered by a particular date. In July the appellant received an offer of $840,000 for the whole of the property. At this stage the agreement with the Township had not been signed nor the plan approved. There was a small flaw in title to part of the land that had to be eliminated before the plan could be registered, and the Township required a bond guaranteeing due performance by the appellant of its contract. In addition a firm estimate of the ultimate costs of the required installations could not be had. In view of these factors the appellant, after attempting without success to have the five acres reserved for the apartment building project excluded from the sale, accepted the offer. Most of the agreements for sale had become void because the plan had not been registered within the time specified. Those not so affected were repurchased by the appellant which permitted the closing of the sale in August 1955.

In assessing the appellant for the year 1956 the Minister treated the whole of the profit realized from the sale of the 50 acres as income from its business. In an appeal from the assessment the appellant contended that a portion of the land so sold had been acquired and held as an investment and that the profit on that portion should be treated as a capital gain.

Held: That at the material time the appellant was engaged in a business of dealing in land and in the course of that business sold a property which though originally in part acquired for an investment purpose had for trading purposes rather than for the purpose of mere realization been dealt with in its entirety as the subject matter of a trading transaction.

2. That in these circumstances the whole of the money received for the property was a trading receipt and the profit thereon a gain made in the operation of the appellant's business in carrying out its scheme for profit making.

3. That the profit was accordingly income within the meaning of the *Income Tax Act* and was properly assessed.

APPEAL under the *Income Tax Act*.

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

E. A. Goodman, Q.C. and *L. A. Schipper* for appellant.

P. M. Troop for respondent.

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THURLOW J. now (May 8, 1962) delivered the following judgment:

This is an appeal from an assessment of income tax for the year 1956. In its fiscal period which ended in that year the appellant realized a substantial profit on the sale of a parcel of land which it owned and in making the assessment the Minister treated the whole of such profit as income from the appellant's business. The appellant's case is that a portion of the land so sold had been acquire and held only as an investment and that the sale of this portion of the land was a mere realization of the investment and the profit attributable thereto not income for the purposes of the *Income Tax Act* but a capital gain.

The appellant was incorporated in September 1953 and obtained title to the land in question in May 1954 under the circumstances to be related. The purchase price was $250,000. The land was sold in a single transaction in July 1955 for $840,000 and the appellant's submission is that of the profit so realized $89,453.05 was attributable to the sale of a particular part of the property which it had acquired and at all material times held for the purpose of erecting apartment buildings thereon to be held for investment purposes rather than for purposes of development and sale.

The lot in question consisted of 50 acres of land in the Township of North York situate about 1,000 feet south of highway 401. It had a frontage of 660 feet on the eastern side of Dufferin Street and extended easterly therefrom for some 3,200 feet. At all material times the land was undeveloped but in January of 1953 when the events to be related began the eastern portion of the lot consisting of about 15 acres lying to the eastward of a proposed extension northwardly of Spadina Road was zoned for single family dwellings while the remaining portion was zoned for multiple family dwellings.

Early in January 1953, A. E. Diamond, an engineer, who, with Joseph Berman was interested in and employed by Cadillac Contracting and Developments Limited, was approached by an agent seeking to sell the property in question which was then owned by Joseph Tanenbaum. Cadillac Contracting and Developments Limited (to which

I shall refer as Cadillac and thus distinguish it from the appellant) was engaged in constructing commercial and residential buildings on developed land. Until that time it had never been concerned in developing land itself, that is to say in subdividing it, providing or arranging for water, sewer and other services, constructing streets and generally making it suitable for building purposes. Nor had Mr. Diamond had experience in that kind of operation. As Cadillac was not in a position to purchase the Tanenbaum land, Mr. Diamond sought to interest several others in it and for that purpose arranged a meeting at which he, Berman, Jack Kamin, a dealer in electrical equipment, Milton Shier, a dealer in hotel and restaurant equipment, and Harold Gross, a machinery merchant, were present. At this meeting it was arranged that the group would try to purchase the land for the purpose of building apartments thereon and keeping them for investment. An agreement was reached regarding the shareholdings of the members of the group and Cadillac was instructed to proceed to take an option on the land on behalf of a new company which was to be incorporated.

By indenture dated January 28, 1953 Cadillac obtained from Tanenbaum for $2 an option exercisable up to April 15, 1953 to purchase the property for $250,000, payment of $225,000 of which was to be secured by a mortgage in favor of Tanenbaum payable two years from the date of closing of the purchase. In the indenture it was provided that when not in default under the mortgage Cadillac should be entitled to obtain partial discharges from the mortgage of portions of the land to the extent of one acre for each $4,500 which Cadillac might pay on account of the mortgage principal prior to maturity. There were however certain express limitations on this right which it is not necessary to set out but which to my mind indicate that the parties were contemplating that the land might during the two year period be or become partially or wholly developed and alienated to other parties whether by way of mortgage or sale or both. It was also provided that the vendor should consent to the registration of a plan or plans of subdivision of the property. The assignment clause at the end of the document was in somewhat unusual form and together

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with the other evidence satisfies me that it was contemplated that Cadillac would assign its rights or some part thereof to the company to be incorporated.

After obtaining the option Mr. Diamond investigated the scheme to build apartments more thoroughly. He checked on the market for this kind of housing and the availability of mortgage money to finance them, on the suitability of the area for multiple family dwellings and in a general way satisfied himself that sanitary sewers and water would become available in due course to enable the development of the land to proceed. He had, however, in reply to an enquiry, received from the Township Engineer of the Township of North York a letter indicating that the land could not be serviced by draining sewage into a sewer which had been constructed for a housing subdivision south of the land in question, and at that time there was no other convenient sewer connection available.

The option was exercised in April 1953 and the transaction was to be closed in May of that year but Tanenbaum refused to complete the transaction and litigation to obtain specific performance ensued. In fact the purchase was not completed until May 1954.

Prior to September 1953 the group met and despite the fact that title to the land had not yet been obtained, retained the services of Cadillac to look after all the work required to have the land ready for building apartments and an understanding was also reached that Cadillac was to build the apartments. Cadillac then retained the services of a firm of town planning consultants to plan the necessary subdivision and also retained an engineering firm to plan the water, sewer, hydro and other services which would be required as a prerequisite to the registration of a plan of subdivision. Without such a plan being registered none of the land could be sold or mortgaged in lots. The provision of storm sewers presented no great problem and it was expected that a water supply would be available in a matter of a few months but sewage disposal presented a major problem and with a view to solving it, various municipal authorities were contacted but without any immediate success. Early in December 1953 application was made in the name of Cadillac for approval of a plan of subdivision of the 15 acres lying to the eastward of the proposed

Spadina Road extension into single family dwelling building lots, these being laid off large enough to permit the use of septic tanks for sewage disposal. The group at that time planned to sell the eastern portion of the property in lots and to develop the western portion for multiple family dwellings. The application for approval of the plan was refused or deferred early in April 1954 on the ground that an adequate supply of water was not yet available in the area. In the meantime the town planning consultants on Cadillac's instructions had prepared 3 alternative tentative subdivision plans for multiple family development of the whole of the area lying between Dufferin Street and the proposed Spadina Road extension but no application was ever made for approval of any of these plans as the problem of obtaining sewer connections had not been solved. Nor was the plan of subdivision of the 15 acre portion resubmitted as it was considered that by the time that water would become available an answer to the sewer problem for the entire property would have been found and in that event, the single family dwelling lots on the 15 acre eastern portion of the property could be smaller in size. Some time later in 1954 an understanding was reached with the Township Engineer under which a connection to a sewer to be constructed northward of the property would be approved if the land or the major portion of it were rezoned to single family dwellings, and in order to get started with their plans it was decided to have most of the land so rezoned, to subdivide the portion so rezoned into single family dwelling lots and to sell the lots if and when the plan was registered but to retain the portion not rezoned and a number of the lots adjacent thereto comprising in the whole about 10 acres fronting on Dufferin Street to await a time when these lots might be rezoned for multiple family dwellings in order to construct apartment buildings thereon. A plan of such a subdivision of all but 1.42 acres of the land was accordingly prepared and submitted for approval in October 1954 and in December 1954 Cadillac was informed that the plan would be recommended for approval by the Minister of Planning and Development subject to compliance with certain alterations and conditions. These included among others a requirement that the appellant convey 11 of the lots to the township and a further requirement that the appellant enter into a contract with

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the township for the construction of the roads and sewers, the installation of services and payment of taxes. A by-law of the township was subsequently passed rezoning most of the property for single family dwellings but the 1.42 acres remained zoned for multiple family dwellings and upon registration of the plan and installation of the sewer and water services it would have been possible to get started with the construction of apartment buildings on it.

At a meeting of the shareholders of the company held on January 29, 1955 it was decided to attempt to repurchase from the township the 11 lots which they would require providing that the price set by the township was below market price, but that if the negotiation of the repurchase of these lots would hold up the sale of the land unduly, the sale of the other lots should proceed without waiting for settlement of a price on the township lots. At the same meeting it was decided that the 1.42 acre lot and lots 152 to 169 which together with the 1.42 acres made up about 5 acres of the land fronting on Dufferin Street would not be put up for sale.

In February 1955 the appellant through several real estate agents proceeded to sell to various purchasers all the lots in the subdivision except the 11 required to be conveyed to the township and those which it had decided would not be sold. The agreements of sale or most of them provided that the sale should be null and void if the plan were not registered by a particular date.

At this stage there were still details to be worked out before the subdivision would be approved, correspondence was still going on with respect to the sewer connection and in view of the proposed construction of a new trunk sewer in the vicinity in a matter of 2 or 3 years arrangements were made for a temporary connection for the appellant's subdivision with the sewer of the subdivision south of the property, but the agreement with the township for the construction of streets and sewers and installation of services etc. had not yet been signed nor had the plan been finally approved or registered when early in July 1955 the appellant received through an agent an offer of $840,000 for the whole of the property. This offer was large enough to yield a profit approximately equal to what the appellant

could expect to realize from the sale of the lots of the subdivision together with a substantial profit as well in respect of the lots which they had not intended to sell. The proposal was considered at a meeting of the directors of the appellant and several factors entered into their decision. There was some flaw in the title to a narrow strip of the land bordering on Dufferin Street which would have to be eliminated before the plan could be registered. Secondly, the township besides requiring the appellant's agreement to construct the streets, sewers etc. required a bond as well guaranteeing due performance by the appellant of its contract. These were difficulties which could be overcome but providing the bond was considered to be something of a burden. In addition the directors were concerned about the ultimate cost of the required installations. Cadillac which was to do the work was prepared only to assure them that its estimates of the costs were realistic but they might fluctuate widely and Cadillac was not prepared to guarantee that the estimates would not be exceeded. These considerations indicated that the subdivision should be abandoned and the offer accepted. On the other hand sale of the whole parcel involved the abandonment as well of their plan to build multiple family dwellings on the land to be held for investment. It was thereupon decided that an effort should be made to see if the purchaser would not buy the property without the 5 acres fronting on Dufferin Street but that if the purchaser required the whole of the property the offer should be accepted provided arrangements could be made for releases from the several purchasers of lots. The prospective purchaser insisted on obtaining the whole 50 acres except the portion required by the municipality for the Spadina Road extension and the property was accordingly sold on July 21, 1955 for $840,000. Most of the agreements of sale of lots had expired or become void because the plan had not been registered in the time limited but it was necessary for the appellant to purchase releases from 2 of the purchasers. This was done at a cost of $7,500 and the sale was completed in August 1955.

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In May of 1955 the appellant had also bought a forty-five acre parcel of land in the Township of Scarboro which it resold a year later at a profit without subdividing the property. These were the only real estate transactions in which the appellant engaged, the profits of the transactions having since then been invested in other companies. The appellant has never had a place of business or employees of its own.

The objects of the appellant company as set out in the letters patent by which it was incorporated include:

> (c) To acquire by purchase, lease, exchange, concession or otherwise city lots, farm lands, mining or fruit lands, town sites, grazing and timber lands and any description of real estate and real property or any interest and rights therein, legal or equitable or otherwise, to take, build upon, hold, own, maintain, work, develop, sell, lease, exchange, improve or otherwise deal in and dispose of such lots, lands, sites, real estate, real property and any houses, apartments or buildings thereon or any interest therein, and to deal with any portion of the lands and property so acquired, subdividing the same into building lots and generally laying the same out into lots and streets and building sites for residential purposes or otherwise; and to construct streets thereon and the necessary sewerage and drainage systems and to build upon the same for residential purposes or otherwise and to supply buildings so erected with electric light, heat, gas, water or other requisites.

I may add that on the evidence I am satisfied that the plan to build apartments was within the financial capacity of the parties interested in the appellant company because of the remarkably small amount of equity capital required, and that the property in so far as it was zoned for multiple family dwellings was purchased for that purpose with intent to realize profits through letting the apartments to tenants, and while I would expect that at that stage each member of the group contemplated the possibilities and probably also assessed to his own satisfaction the prospects both of selling the apartments some day at a profit and of selling the land at a profit if the plan to erect apartments failed, I do not regard the situation as one in which it should be inferred that the group would have purchased or did purchase the property as a speculation looking to resale or that the group when purchasing the property intended to turn it to account for profit by any method that might be considered expedient including resale, though as events turned out that appears to me to describe what they did with it.

For the present purpose the relevant provisions of the *Income Tax Act* R.S.C. 1952, c. 148 are sections 3, 4 and 139(1)(*e*) which provide 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.

The problem to be determined is whether for income tax purposes the whole of the profit realized by the appellant on the sale of the Tanenbaum property was income from its business within the meaning of these provisions, without any deduction therefrom being made in respect of such portion of the profit as could be regarded as attributable to the sale of the 5 acres fronting on Dufferin Street.

The test to be applied for resolving the question is that stated in *Californian Copper Syndicate v. Harris*[1] where the Lord Justice Clerk after speaking generally of the distinction between a gain which was not assessable to income tax and a gain from a trade which was assessable and after giving the buying and selling of lands or securities speculatively in order to make gain as the simplest example of what is trading said:

> 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 seeking an answer to this question it is I think necessary to have regard to the whole of the facts of the particular case and not merely to some of them though of course not all of them may be of equal importance. The present case for example is not to be regarded as one in

[1] (1904) 5 T.C. 159 at 166.

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which the only material facts are that a property was purchased, or purchased in part, for an investment purpose and subsequently sold for more than the appellant paid for it. There is much more to the picture than that and in reaching a conclusion the other features of the situation must be considered as well.

The appellant is a corporation the objects of which are broad enough to include among others carrying on business for profit both by acquiring and holding investments in real estate and by dealing in real estate and, as I view the evidence, from the time of its acquisition of the Tanenbaum property in May 1954, if not earlier, the appellant had property, consisting of the eastern 15 acres of the property, which it had acquired for the purpose of development and sale and was engaged in a business which at least included developing and dealing in land. I am also of the opinion that the sale of the property made in July 1955 was a sale in the course of that business. Insofar as the transaction involved the sale of the forty-five acres or thereabouts which had been subdivided into lots for the purpose of sale, the fact that the agreements of sale to purchasers were abandoned and the property sold in a single transaction—in which all the effort which had been put into the subdivision of the land came to naught—would not in my opinion make such sale any the less a sale in the course of the appellant's business of dealing in land and more particularly do I think this is so in view of the fact that the decision to accept the offer was based on considerations relating to the trading activities of the appellant and that in order to take advantage of the offer the appellant took steps to obtain releases from two purchasers and thus "matured" the property for the purpose of carrying out the particular transaction. The only feature which has given me any doubt on this aspect of the matter is the question of whether the inclusion in the transaction of the 5 acres which were not formerly for sale could (assuming these to have been at that time an asset of a capital as opposed to one of a trading nature) on the principle of *Doughty v. Commissioner of Taxes*[1] stamp the whole transaction as one outside the scope of the appellant's business. I do not however think, even on that assumption, that such is the

[1] [1927] AC. 327.

effect of including the 5 acres in the transaction for the completion of the transaction did not put the appellant out of the business of dealing in real estate since it then had on hand the Scarboro property which so far as appears was not acquired for any purpose other than that to sell it for a profit—which was what was ultimately done with it—and the transaction itself in which the Tanenbaum property was sold was in no sense a slump sale of an undertaking but simply a sale of land which was a kind of transaction characteristic of a business of dealing in land.

But finding as I do that the sale of the Tanenbaum property was a transaction in the course of the appellant's business of dealing in land appears to me still to leave not satisfactorily answered the question why any profit attributable to the 5 acre portion of the property which had not previously been for sale should be regarded as profit from the business since I do not think it necessarily follows as a matter of course that because the 5 acres (assuming still that they were in a different category from the rest of the property) were sold in a transaction of the appellant's business, the sum received therefor could not be regarded as a mere realization of the value of the 5 acres. The answer however in my opinion appears from the transaction itself and the circumstances surrounding it and in particular the reasons why the property was sold.

It can I think be regarded as established as a general proposition that the mere fact that a property has been purchased without any intention of making profit by reselling it will not necessarily result in any sale subsequently made being a mere realization rather than a sale in an operation of business in carrying out a scheme for profit making. Thus in *Cooksey and Bibbey v. Rednall*[1] where the appellants had bought a farm for farming purposes and sold it 14 years later and had been assessed on the profit realized on the sale, the appellants having in the meantime been engaged in trading in land, Croom-Johnson J. in the course of a judgment allowing the appeal said at page 519:

> I have no doubt that if there had been evidence here that at some time after the original purchases of a lot of this property these two gentlemen together had gone in for a system of land development with regard to that or part of it, it would have been open to the Commissioners to find that they had turned what had been an investment into

[1] (1949) 30 T.C. 514.

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the subject-matter of a trading in land. It does not follow necessarily that they would so find, because it may be that the Commissioners would come to the conclusion that the partnership had not traded but was merely realising a capital asset. Everything must depend on the exact circumstance.

Again in *Dunn Trust Limited v. Williams*[1] Vaisey J. in a judgment reversing the Commissioners' finding that the profits from certain sales of shares arose from the company's trading in shares said at page 273:

> First of all, we have the definite finding that these shares were purchased in 1940, not with the intention of dealing in those stocks and shares, but with the object of finding a permanent investment—or at least, the word "permanent" is not used, but an investment of a portion of the company's reserves. Now, that finding of the General Commissioners undoubtedly involves this, that that object and that intention must have been departed from; but there was no evidence to show how or when or by whom it was departed from, and I have the greatest difficulty in discovering how or when or by whom the General Commissioners decided that that change of object, and that change of intention, had been effected. That is the first thing.
>
> The finding that these stocks or shares had been purchased with that object seems to me to be a finding which, in order to justify the conclusions of the General Commissioners, must have been followed by a further finding that at some time, in some manner, by some operation or other, the object had been reversed and the intention fundamentally altered.
>
> So far, I have found it very difficult to discover upon what the General Commissioners can have based the decision that the realisation of these shares produced profits out of the trading of the company. Then, when I look at the statement of the sales which resulted in producing the profits which have been held to be the subject of tax, I find, as I have already stated in passing, explanations given as to why and how and for what purpose these shares were sold; and I find that the purposes indicated are quite inconsistent with the purposes which should animate those who direct the fortunes of a trading company when they are effecting sales of that company's stock-in-trade, be it investments or be it any other kind of property; because I find that the General Commissioners go out of their way to state, not that the securities were disposed of in the ordinary course of business or because they thought that that would produce a desirable profit, or because they thought that it was a trading operation which was financially beneficial to the company, but I find the statement that they were disposed of under the circumstances which are set out in the stated case.
>
> These circumstances were as follows. First, in one case, Mr. Kerman ceased to be associated with the management of the company whose shares were in question, and the control had changed,
>
> > "whereon it was decided [presumably by the board of directors, or by the managing director] not to continue to hold the shares of the company".

[1] [1950] T.R. 271.

That seems to me to be a statement which is almost a direct negative of the ordinary and inevitable and common-form motive which actuates the mind of those who are dealing with the stock-in-trade of a trading company. Then, with regard to certain other investments, another block of these holdings, the stated case says:

> "After the death of Mr. Kerman, it was decided that these shares were not suitable investments [not that they could be productively sold, or turned to good account by being sold at a profit, but that they were not 'suitable investments', which I agree is an ambiguous expression] and these shares were *accordingly* sold"

—"accordingly". Finally, the last item was the small sum received on the liquidation of the Chosen Corporation, which was of no significance, because that was a sum which the company had no option to refuse, and which came to it, so to speak, without any active decision on the part of the company.

In that case it was apparent that the first two sales of the shares were made for simple realization motives alone and in the third case the company whose shares were held had gone into liquidation and the realization was brought about without any decision by the taxpayer.

The situation is different here. There was first of all no desire to realize the company's investment in the 5 acres and no occasion for doing so apart from the considerations which led to the decision to sell. Secondly, apart from the attractiveness of the offer those considerations, being concerned with the subdivision project, were all related to the trading aspect of the appellant's affairs and none, save the difficulty in the title, had any relation to the 5 acres or the plan to build apartments thereon. In my view the sale of the 5 acres in these circumstances cannot be dissociated from the trading considerations which prompted the sale of the whole property. (*Vide Atlantic Sugar Refineries v. M.N.R.*)[1].

Finally, whatever may have been the intention of the group with respect to the property at the time of its purchase, it is apparent that the intention with which it was bought was a flexible one and that it changed from time to time while the property was held. At the outset the plan was to subdivide and sell the eastern 15 acres and to develop the remaining 35 acres by building apartment buildings to be held for investment. When it turned out that this plan involved delay, the purpose changed and it was decided to subdivide and sell all but 10 acres of the land and to build apartments on 10 acres only. This alone was a

[1] [1948] Ex. C.R. 622; [1949] S.C.R. 706.

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considerable change of the original scheme but the scheme was still further altered when the decision was made to retain only 5 acres for the investment purpose. The decision to subdivide into single family dwelling lots and sell 30 of the 35 acres originally intended for apartments was based simply on business considerations relating to the question of how best to turn the property to account for profit, for nothing prevented the group from waiting until sewer capacity became available to serve apartment buildings on the whole 35 acres except the practical considerations of the loss and expense attending the holding of the land for an uncertain period, and the uncertainty as to what the market for apartment space might be when that time came. When this decision had been reached, a new plan of subdivision was prepared and the scheme proceeded to the point where ultimately the lots were sold subject always to the registration of the plan. Had the plan been registered and these sales completed there would I think be no doubt that profit from them would have been income and yet the intention at the time of purchase with respect to the land so subdivided and sold had been the same as that which the group had for the 5 acres. I think that such profit would have been income because the land so subdivided and sold had become the subject matter of a trading in land. The next change of intention did not involve the preparation of yet another plan of subdivision but in effect involved simply the abandonment of all that had been done and the sale of the whole property but it too was dictated by practical considerations concerned in my view entirely with the trading activities of the company. Regardless of what had been intended earlier, when this decision was made and carried out the property in my opinion was being dealt with as a single trading asset with a single trading intention with respect to the whole of it and I can see nothing about the transaction or the circumstances in which it was carried out which establishes or even suggests that the appellant's investment in the property, insofar as it can be said to have related to the 5 acres, was merely being realized. By the time the offer was accepted that too had become part of the subject matter of a trading in land.

The situation as I view it is thus one in which at the material time the appellant was engaged in a business of dealing in land and in the course of that business sold a

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property which though originally in part acquired for an investment purpose had for trading considerations rather than for the purpose of mere realization been dealt with in its entirety as the subject matter of a trading transaction. In these circumstances the whole of the money received for the property was in my opinion a trading receipt and the profit therefrom a gain made in the operation of the appellant's business in carrying out its scheme for profit making. The profit was accordingly income within the meaning of the *Income Tax Act* and was properly assessed.

The appeal therefore fails and it will be dismissed with costs.

Judgment accordingly.

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Jan. 15

Feb. 7

BETWEEN:

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

AND

ALBANI THIBAULT ..... RESPONDENT.

Revenue—Income—Income Tax—Admissibility of evidence to vary sale price of property set out in deed—Appeal from Tax Appeal Board a trial de novo—Presumption of validity of assessment on appeal from Board's decision—Quebec Civil Code, art. 1234—The Income Tax Act, R.S.C. 1952, c. 148, s. 100(3).

On an appeal from an assessment to the Tax Appeal Board the respondent contended that the $12,000 added by the Minister to his taxable income was a non-taxable capital gain. He submitted that the sum formed part of the sale price of a property sold by him by notarial deed in which the consideration therein stated to be $68,000 was in fact $80,000. The $12,000 difference he claimed was paid him by the purchaser on the signing of the deed before the notary. The Minister objected to the admission of oral evidence to vary the terms of a written document. The Board allowed the respondent to call witnesses in support of his allegations. It also heard the purchaser deny the making of the $12,000 payment. On an appeal by the Minister from a finding in favour of the respondent.

Held: That the rule under the *Civil Code* (art. 1234) which forbids the use of oral evidence to contradict or vary the terms of a valid written instrument applies only as between the parties to it and not to third parties for whom the instrument falls into the category of *res inter alios acta*.

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2. That the hearing of an appeal from a decision of the Tax Appeal Board by the Exchequer Court is a trial *de novo* and it is for the court to base its decision on its own evaluation of the evidence.

3. That as the evidence adduced by the respondent failed to displace the presumption as to the validity of the assessment, or to remove the serious doubts the court entertained concerning the respondent's allegations, the appeal should be allowed and the assessment affirmed.

APPEAL from a decision of the *Tax Appeal Board.*

The appeal was heard before the Honourable Mr. Justice Dumoulin at Chicoutimi.

Maurice Paquin, Q.C. and *Rolland Boudreau* for appellant.

Roland Fradette, Q.C. for respondent.

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

DUMOULIN J. now (February 7, 1962) delivered the following judgment:

Le Ministre du Revenu national interjette appel devant cette Cour d'une décision de la Commission d'appel de l'Impôt sur le revenu[1] qui annulait la cotisation supplémentaire émise, le 9 décembre 1958, par le Ministre du Revenu national, et ajoutait un montant de $12,000 au revenu de l'intimé pour l'année d'imposition 1956.

Le 15 mai 1957, M. Thibault produisit une déclaration d'impôt pour l'année 1956, comportant un revenu réel de $1,724.75 qui, conformément aux exemptions statutaires, échappait à toute imposition. Consignons de suite que le Ministère du Revenu national avait autorisé ce contribuable à computer son revenu annuel selon la méthode dite: d'augmentation de capital. Pour l'exercice fiscal terminé le 31 décembre 1956, le capital déclaré de l'intimé s'était accru d'une somme de $44,000, comme il appert aux états financiers annexés à la déclaration réglementaire.

Cet accroissement provenait, était-il dit, du profit réalisé sur la vente d'un immeuble situé dans la ville de Port-Alfred.

Les parties admettent que le prix coûtant de cette construction fut de $36,000, et le prix apparent de sa revente de $68,000. Cette dernière transaction, conclue le 19 juin 1956, entre Richard Gagnon de Jonquière, en qualité

[1] [1961] 61 D.T.C. 378; 27 Tax A.B.C. 52.

d'acquéreur, et l'intimé, comme vendeur, fut consignée dans un acte authentique devant le notaire Jules Gauthier, à Jonquière, P.Q. La complication provient de ce que le bénéfice réel de cette mutation de propriété ne pouvait dépasser le chiffre de $32,000, si l'on s'en rapporte à l'acte authentique de vente, laissant de la sorte un excédent inexpliqué de $12,000 entre le coût originel de $36,000, un prix vendant de $68,000 et une totalisation déclarée de $80,000. Le débat ici engagé a porté uniquement sur des questions de droit, la transcription des témoignages devant la Commission d'Appel de l'Impôt étant versée de consentement au dossier. Il est également admis que l'appel devra être rejeté si la preuve orale soumise par l'intimé justifie sa prétention que le montant controversé de $12,000 lui fut payé en billets de banque par l'acheteur Gagnon, en présence du notaire Gauthier, lors de la conclusion de la vente, dont le prix véritable serait alors, non pas de $68,000, mais bien de $80,000.

A l'appui de cette prétention, l'intimé s'est efforcé d'accréditer, au moyen de son témoignage et par l'audition de quelques témoins, l'existence d'une entente préalable selon laquelle l'acheteur lui verserait au comptant une somme de $12,000, ce qui aurait été effectué, comme susdit, chez le notaire Gauthier, le 19 juin 1956. Par contre, Richard Gagnon, l'acquéreur, niera catégoriquement cette allégation et s'en tiendra au prix stipulé dans l'acte.

Abordons maintenant l'examen critique de cette preuve formellement contradictoire.

Le notaire Jules Gauthier, exerçant en la ville de Jonquière, figure en tête de liste des témoins. Le savant commissaire de l'Impôt, Me Maurice Boisvert, c.r., après avoir permis sous réserve la preuve orale, objection qui sera traitée plus loin, demande au notaire s'il se souvient qu'au moment de la signature de l'acte, une enveloppe ou un paquet contenant de l'argent aurait été remis par l'acheteur, Richard Gagnon, au vendeur, Albani Thibault, en sus de la somme de $68,000, stipulée au contrat. A quoi le notaire répond: "Je crois que oui. Actuellement, je ne m'en souvenais pas, mais je crois que oui".

Autres questions posées par Me Fradette, c.r., procureur de l'intimé (cf. transcription des témoignages, p. 47):

D. Est-ce que le contenu de l'enveloppe a été vidé?

R. Non.

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D. Vous savez qu'une enveloppe a été remise?
R. Oui.
D. Est-ce qu'elle était volumineuse?
R. Je ne le sais pas.

Puis, à la page 49, nous lisons que l'avocat de l'appelant, Me Paquin, c.r., contre-interrogeant Me Gauthier, lui demande:

D. Vous avez répondu tantôt à une question que vous croyiez qu'une enveloppe ou un paquet . . .
R. Je croyais, oui; sur le moment je ne m'en souvenais pas. Mais quand je suis venu à penser à tout ça, je crois qu'il y a eu quelque chose comme ça.

Me Fradette revient à la charge (p. 50):

D. Vous avez remis à monsieur Thibault une enveloppe?
R. Oui, à monsieur Thibault.

Par Me Paquin, encore (pp. 56 et 57):

D. Pouvez-vous jurer que vous avez eu une enveloppe?
R. Écoutez . . . Je ne voudrais pas . . . Je sais qu'il y a eu quelque chose; je ne voudrais pas dans ce sens-là . . . Quand on fait un acte de cette importance-là, à présent, il y a des choses, des accessoires qu'on ne regarde pas. Je suis certain que s'il m'a remis de l'argent, je l'ai compté et je l'ai remis à mon comptable; c'est-à-dire, je ne compte pas l'argent, j'ai un homme pour ça.
D. Vous supposez qu'il y a eu une enveloppe mais vous ne savez pas ce qu'il y avait dedans?
R. Je l'ignore complètement.
D. A votre connaissance personnelle, il y a eu une autre considération que celle indiquée au contrat que vous avez reçu?
R. Je m'en tiens à mon acte.

L'impression que dégage cette hésitante relation du notaire, qui ne se souvient pas, qui pense, croit, suppose, en est une de complète imprécision. Me Gauthier estime effectivement avoir remis à Thibault une enveloppe, dont il ignore complètement le contenu, n'ayant pas ouvert ce pli en présence des parties. Le notaire, en définitive, s'en tient à son acte, (pièce A-1) attitude prudente, vu ses vacillations de mémoire et la contradiction que lui oppose l'agent d'immeubles, Jean-Paul Mongrain, mandataire de Thibault pour cette transaction. Mongrain, on le constatera à l'instant, est très catégorique quant à la production par le notaire du contenu de ce qui, pour le premier, était une enveloppe, et pour le second, un sac.

A la page 54 de la transcription officielle, nous trouvons la réponse ci-après à une question du savant commissaire, Me Boisvert. Mongrain soutient que:

R. . . . le notaire a apporté un sac et puis, évidemment, il fallait voir ce qu'il y avait dans le sac, et il a jeté le sac sur son bureau.

D. Qu'est-ce qui a été sorti du sac?

R. Il y avait plusieurs liasses de billets de banque; il était supposé y avoir $12,000.

Le témoin réitère cette assertion à Me Fradette, qui lui demande (p. 59):

D. Et il a vidé le contenu sur le bureau?

R. Oui, pour constater que c'était de l'argent là-dedans.

D. C'était en paquets?

R. En liasses.

J'éprouve une certaine difficulté à concilier ces témoignages divergents, on en conviendra, du notaire Gauthier, et du courtier en immeubles, Mongrain, que l'éthique professionnelle ne semble pas étouffer, puisqu'il reconnaît avoir coupé l'herbe assez rase sous le pied de son confrère, Gaston Girard, détenteur depuis le 29 mars 1956 d'un mandat écrit de négocier la vente éventuelle de l'immeuble. Cette procuration dûment signée par Albani Thibault porte la cote A-3.

Jean-Paul Mongrain relate que les pourparlers préliminaires, puis la conclusion des conditions de vente, eurent lieu au camp de pêche de Thibault, hôte, à ce moment-là, de Gagnon et du témoin.

Cet agent d'immeubles n'est guère plus précis dans son témoignage que ne le fut le notaire Gauthier et, à mon sens du moins, n'élimine pas l'incertitude qui plane toujours sur la supposée promesse qu'aurait engagée Gagnon de verser $12,000 à son vendeur, outre le prix indiqué au contrat. Mais voyons plutôt, à la page 53, par Me Fradette:

D. A quel prix aviez-vous convenu de vendre l'immeuble à Richard Gagnon?

R. Il y a eu une discussion à ce sujet-là, je crois, je ne suis pas positif exactement de ce qui est arrivé, mais ils se sont entendus, monsieur Thibault et monsieur Gagnon, par la suite. La vente a dû se faire pour environ $80,000.

A la page 56, Mongrain encore répond au savant membre de la Commission d'Appel, qui lui demande:

D. Étiez-vous présent quand il y a eu entente pour le prix de vente?

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R. «Entente ...» J'ai dit ce qui était arrivé chez le notaire; ça veut dire que c'est la fin de l'affaire. Il y a bien des discussions qui se sont passées. Je ne me rappelle plus exactement de ce qui s'est dit; ça fait assez longtemps.

A la page 65, c'est toujours Me Boisvert, c.r., qui interroge Mongrain:

D. A-t-il été question, devant vous, au camp là-bas, que le prix serait de douze mille piastres de plus que $68,000?

R. Il a été, devant moi, du côté de monsieur Thibault, il a toujours été décidé que l'immeuble ne se vendrait pas à moins de $80,000, et je connaissais monsieur Thibault. Je n'ai même pas essayé de le faire changer d'idée parce que je les ai laissés se débattre.

D. Son prix minimum était toujours d'au moins $80,000, devant vous?

R. Oui, au moins $80,000.

D. Maintenant, a-t-il été question entre eux, devant vous, qu'un montant serait payé et que ce montant ne figurerait pas dans l'acte authentique qui devait être signé devant le notaire?

R. Peut-être que ç'a été dit devant moi ou que je l'aurais entendu dire, mais je ne me rappelle pas exactement qui me l'a dit.

D. Est-ce un des deux?

R. Oui, certainement un des deux, mais je ne sais pas lequel parce que je ne peux pas me rappeler.

D. Le pourquoi de cette opération-là, est-ce qu'il en a été question devant vous?

R. Non.

Il ne paraît pas exagéré de tenir qu'une narration aussi vague ne tende à établir que l'une des deux conjectures suivantes: Mongrain n'a eu connaissance de rien autre que de la seule vente de l'immeuble, ou il évite de rapporter, avec suffisante clarté, ce qu'il pourrait savoir. Bien que l'indice régulier de sa commission, comme agent vendeur, fût de 5%, Mongrain se contenta d'une rémunération de $1,000 parce qu'un autre courtage dut être payé à un premier agent, Gaston Girard, déjà détenteur du mandat de Thibault.

Un dernier incident, digne de mention, dissipe le médiocre degré de créance qu'auraient pu m'inspirer encore les dires de Mongrain. Quand les choses commencèrent à tourner à l'aigre avec les fonctionnaires de l'Impôt fédéral, Mongrain fut instamment requis par Albani Thibault d'assermenter un affidavit, daté le 31 août 1957, (pièce I-1) dont voici les deux paragraphes pertinents:

1. Vers le 20 juillet 1957 j'ai assisté à la signature d'un acte de vente par M. Albani Thibault à M. Richard Gagnon d'un immeuble situé à Port-Alfred au coin de la 1re rue et de l'avenue du Port.

2. J'ai vu alors le notaire Jules Gauthier de Jonquière, où s'est signé le contrat, remettre à M. Albani Thibault un sac en papier contenant une somme de $12,000 en billets de banque du Canada, laquelle somme a été vérifiée sur place.

Cette solennelle attestation incita le savant procureur de l'appelant, Me Paquin, à contre-interroger Mongrain et à lui poser entre autres certaines questions relativement à la vérification du contenu du sac-enveloppe. Lecture faite du 2e paragraphe de l'affidavit ci-haut relaté, et à la page 67 de la transcription des témoignages, l'avocat de l'intimé ajoute:

D. . . . Est-ce que ç'a été vérifié?

R. On ne vérifiait pas billet par billet, mais on pouvait être certain qu'il n'y avait pas une grosse différence.

D. Tantôt vous avez dit que vous ne vous souveniez pas combien il y avait dans le sac?

R. Si j'avais compté les billets, billet par billet, évidemment que j'aurais été plus affirmatif.

D. A la demande de qui avez-vous signé cet affidavit?

R. De monsieur Thibault.

D. Est-ce que vous êtes déjà allé avec monsieur Thibault au bureau de l'Impôt à Québec?

R. Oui, j'y suis déjà allé.

D. Relativement à cette affaire?

R. Oui.

D. N'est-il pas vrai que, à ce moment-là, vous refusiez de signer un affidavit?

R. J'ai toujours refusé jusqu'à un certain moment, oui.

D. Pour quelle raison?

R. La raison . . . Je n'aime pas bien cette affaire-là.

Nous lisons enfin à la page 68, par Me Paquin:

D. Est-ce que vous auriez demandé de l'argent à monsieur Thibault?

R. J'ai demandé plusieurs fois à monsieur Thibault de me prêter de l'argent et il m'en a prêté plusieurs fois.

D. Pour signer l'affidavit?

R. Non, je n'ai jamais demandé d'argent à monsieur Thibault pour signer quelque chose. Seulement, j'ai pu lui demander de me prêter de l'argent. Entre demander un paiement et emprunter, c'est une autre affaire.

L'intimé, Albani Thibault, entendu à la suite de Mongrain, affirme ce que nous savons déjà: une prétendue stipulation à l'effet que Richard Gagnon lui verserait de la main à la main $12,000 outre le chiffre de $68,000 indiqué au contrat.

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Ce déposant dit encore que, pendant le trajet de retour à son domicile, il aurait remis $800 à Mongrain, après s'être remboursé de $200 que ce dernier lui devait. Puis l'argent aurait été minutieusement recompté chez Thibault en présence de son épouse qui témoigne au même effet. Cette vérification révélant un moins payé de $20, Gagnon en fut informé et vint parfaire ce reliquat. Gagnon reconnaît cette prestation d'un dernier billet de $20, afin de corriger une méprise involontaire, mais persiste toutefois à dire que la somme ainsi complétée n'en était pas une de $12,000, mais bien de $500, pour l'acquisition d'un droit de pêche au lac des Ha! Ha!

Mentionnons qu'un second recomptage des billets de banque se serait effectué en présence du jeune fils de Thibault. Enfin, deux jours plus tard, le 21 juin, Thibault déposait à la banque de Montréal, succursale de Port-Alfred, 52 billets de $10, 459 de $20, 10 de $10 et 12 de $100, au total, $11,000. Le bordereau du dêpôt et la feuille du régistre bancaire, où se lit la position de compte de l'intimé ont été produits sous les cotes respectives de I-3 et A-4.

Durant les 48 heures qui précédèrent, les liasses de papier-monnaie furent placées dans le coffre-fort que l'intimé gardait chez-lui pour les fins de ses affaires. La présence de ce meuble de sûreté permet de supposer la réception occasionnelle par Thibault de sommes considérables d'argent. Aurions-nous là une indication de la provenance réelle des $11,000? Cette conjecture ne me paraît pas insoutenable dans les circonstances du cas.

Les affirmations de Thibault, même étayées en apparence, et après l'événement, sur la corroboration de sa femme et de son fils, qui n'étaient pas présents chez l'officier public, puis sur l'entrée à son compte de banque de billets au montant de $11,000, me laissent perplexe si je les confronte avec l'unique motif puéril et dérisoire que ce témoin rapporte comme mobile déterminant de l'entente accessoire au contrat. Cette explication se trouve au bas de la page 76, la voici:

> Richard Gagnon a dit: «Je vais te donner douze mille piastres en argent et je vais te faire un contrat de $68,000, par rapport que ça coûte moins cher de contrat quand le contrat est moins haut. Quand la vente est moins haute, ça coûte moins cher.»

Nous savons déjà que Richard Gagnon, le témoin suivant, nie énergiquement le prétendu paiement de $12,000. Il convient du paiement à Thibault, chez le notaire Gauthier, de $500 pour les fins ci-après (pp. 103 et 104):

R. . . . Je suis allé voir monsieur Thibault chez lui et je lui ai demandé de me faire bénéficier, par le fait que j'étais amateur de pêche, d'un droit de club. Il m'a proposé de me vendre un droit avec chalet pour $3,000. Monsieur Mongrain et monsieur Thibault étaient là. J'ai refusé parce que j'ai dit que c'était trop cher pour moi. Lorsque nous nous sommes entendus sur le prix définitif de l'immeuble, j'ai demandé à monsieur Thibault: «Est-ce que vous accepteriez de me vendre une part du club?»

D. Quel était le prix convenu?

R. $68,000. Et monsieur Thibault m'a dit, exactement, en autant que je puisse me rappeler de ses paroles, et je crois m'en rappeler pas mal, monsieur Thibault m'a dit: «Pour ce droit de pêche-là, je peux bien te l'accorder, mais comme il n'y a pas de comptant sur l'immeuble . . .—parce qu'il y avait trois mille piastres que je devais verser, selon l'entente— . . . il faudrait que tu me payes parce qu'il faut que je paye la commission de l'agent d'immeuble, et ce serait normal que je te demande une somme de cinq cents piastres.»

Il importe de préciser que ce versement de $3,000 ne devenait dû que le 1er juillet 1957 et ne portait pas intérêt.

Point n'est besoin de longs commentaires à l'endroit de ce témoignage qui, je le répète, fut la contrepartie absolue de celui de l'intimé. Je soulignerai cependant un dernier passage où Richard Gagnon rapporte une demande que lui aurait faite le vendeur Thibault (pp. 106 et 107):

. . . Il m'avait expliqué alors que sur son bilan d'impôt de 1956 il manquait une somme de dix mille dollars pour être capable de justifier son rapport d'impôt. Alors, il m'a demandé si j'avais objection à ce que je déclare la vente de l'immeuble qu'il m'avait vendu au prix de $78,000 au lieu de $68,000. Il m'a dit: «Tu n'as pas même la peine de t'occuper de la chose. Moi, ça va me donner une grosse chance et ça ne lie personne.»

Pour peu que l'on compare cette raison qui, eût-elle produit le résultat espéré, épargnait à Thibault une taxe de $3,259.60, comme on le constate à la lecture de l'article 9 de l'avis d'appel, ne doit-on pas logiquement lui reconnaître beaucoup plus de plausibilité qu'à l'hypothèse d'une réduction de quelques dollars des honoraires du notaire Gauthier, selon la prétention de l'intimé.

A ce stade de mes notes, il me faut apporter certains éclaircissements quant à la façon dont la cause me fut présentée par les procureurs des parties. Le débat se déroula presque tout entier dans le champ clos de l'article 1234 du

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code civil, sans analyse contradictoire de la preuve testimoniale. Autrement dit, j'eus l'impression très nette que l'unique nœud à trancher n'était autre que l'admissibilité de la preuve orale et, advenant une solution affirmative, que la prépondérance de la preuve favorisait l'intimé.

Ce sentiment que, d'une part, la preuve devant la Commission d'Appel de l'Impôt n'était pratiquement pas remise en question, et, d'autre part, mon opinion assez tôt formée de l'inopposabilité, en l'occurrence, de l'article 1234, me causèrent une impression très différente de celle à laquelle j'en arrive aujourd'hui.

Au début de mes remarques, j'ai mentionné une longue controverse soutenue devant le commissaire de l'Impôt et reprise lors de la re-audition de cette affaire en ma présence. Ce débat se résume à peu de choses; quelques mots en disposeront. L'appelant invoque, à l'encontre de toute preuve testimoniale, l'article 1234, qui interdit de recourir à la preuve verbale pour contredire ou changer les termes d'un écrit valablement fait. Il paraît élémentaire de rappeler que ce texte restrictif ne vaut qu'entre les parties à l'acte et ne s'applique nullement aux tiers pour qui tel écrit tombe dans la catégorie de la *res enter alios acta.* Or, en l'occurrence, les parties ne sont plus Gagnon et Thibault, mais celui-ci et le Ministère du Revenu national du Canada.

Et encore, il ne s'agit point de contredire ni de changer un iota à l'acte authentique de vente, mais de tenter d'établir l'existence d'une convention séparée, savoir le paiement au comptant de $12,000. Toutefois, je n'insiste pas sur ce point et je me limiterai à citer deux lignes de Mignault (*Droit Civil Canadien*—P.-B. Mignault, Vol. VI, p. 86.) qui me paraissent concluantes sur le sujet, les voici:

> Ajoutons que les tiers peuvent prouver à l'encontre d'un écrit qu'on leur oppose par tout genre de preuve.

Gagnon seul était recevable à se prévaloir de l'article 1234, contre Thibault.

Conséquemment, s'il est exact de tenir que l'appelant soit un tiers, à l'égard de cet acte authentique, il ne saurait s'insinuer au lieu et place des signataires pour se réclamer des fins de non-recevoir dont ceux-ci pouvaient faire état. Je ne vois donc pas que la recevabilité de la preuve orale soit en rien restreinte ici.

Il reste que je dois opter pour l'une ou l'autre des thèses divergentes.

Bien que la loi fiscale qualifie officiellement d'appel l'excipation devant cette Cour d'une décision de la Commission d'Appel de l'Impôt, plusieurs jugements ont reconnu à telle procédure le caractère d'un nouveau procès (trial *de novo*). Qu'il me suffise de référer les parties à la cause suivante: *The Minister of National Revenue v. Simpson's Limited*[1], où l'honorable J.-T. Thorson, président de cette Cour, décrit ainsi la position des litigants dans les instances d'appel des décisions de la Commission de l'Impôt sur le revenu:

Held: That the hearing of an appeal from a decision of the Income Tax Appeal Board to this Court is a trial *de novo* of the issues of fact and law that are involved and the hearing in this Court must proceed without regard to the case made before the Board or the Board's decision.

Le langage même de la loi de l'Impôt sur le revenu, (S.R.C. 1952, C. 148), à l'article 100, sous-paragraphe 3, prend soin de spécifier que:

(3) Sur production des pièces mentionnées aux paragraphes (1) ou (2) et de la réplique requise par l'article 99, l'affaire est réputée une *action* devant la cour et, à moins que cette dernière n'en ordonne autrement, prête pour audition.

Les normes d'appréciation auxquelles défèrent les tribunaux d'appel et ceux de première instance diffèrent considérablement. Dans le premier cas, le ou les juges n'ont qu'à se demander si un jury, correctement éclairé sur les questions de droit, eût été fondé à rendre tel verdict en fonction de la preuve, quelle que soit leur opinion personnelle. Mais le juge qui préside à un nouveau procès demeure l'arbitre absolu de la preuve et doit baser sa décision sur la version qui lui semble offrir une crédibilité prépondérante.

Quel avantage pratique Richard Gagnon, acquéreur de l'immeuble, pouvait-il entrevoir en dissimulant le prix réel de cette transaction? Je m'interroge vainement à ce sujet et j'incline à penser qu'il lui eût mieux valu admettre un coût d'achat de $80,000 afin de réclamer, annuellement, une dépréciation proportionnée. Par ailleurs, Albani Thibault évitait une imposition supplémentaire de $3,259.60, si l'indice de cette mutation de propriété était fixé à la somme de $80,000.

[1] [1953] Ex. C.R. 93.

1962

MINISTER OF NATIONAL REVENUE v. THIBAULT

Dumoulin J.

C'est un puissant facteur; il s'en trouve d'autres que je pense avoir précédemment mis en lumière, et qui consistent dans le quasi-mutisme du notaire instrumentant, dans les incohérences, les réticences et les contradictions du témoin Mongrain.

Le prêt d'argent que Thibault consentit à Mongrain quand celui-ci souscrivit l'affidavit, pièce I-1, n'ajoute certes pas à la valeur de ce témoignage.

Finalement, Gagnon déclare qu'au moment de son acquisition de l'immeuble il était âgé de 26 ans et ne possédait pas alors, et n'a point réalisé depuis, des économies de $12,000, et qu'il n'a contracté aucun emprunt à l'occasion de cette transaction immobilière.

Par tous ces motifs, je suis d'avis que l'intimé, auquel incombait le soin de repousser la présomption militant en faveur de la cotisation ministérielle, n'a pas réussi à soumettre une preuve plus satisfaisante que celle de son adversaire, et n'a pas dissipé le doute sérieux que j'éprouve à l'endroit de ses prétentions.

En conséquence je dois accueillir l'appel, et déclarer bien fondée la recotisation du 9 décembre 1958, qui ajoute une somme de $12,000 au revenu de l'intimé pour l'année d'imposition 1956.

L'appelant aura droit de recouvrer ses dépens de Cour après taxation.

Jugement conforme.

1961

Apr. 11

1962

May 2

BETWEEN:

EDOUARD GALIPEAU .....APPELLANT;

AND

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

Revenue—Income—Income Tax—Garage mortgaged to oil company—Credits granted garage owner undertaking to deal exclusively in company's products—Capital or Income—The Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4 and 139(1)(e).

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The appellant, a garage and service station operator, mortgaged his property to Imperial Oil Ltd. to secure a loan of $49,600 to be used in expanding his business. The mortgage provided that the property should continue to be used as a garage and service station and that the appellant should deal exclusively in Imperial Oil products to be supplied to him at the regular price to retailers in force at the time of each purchase. In the event of appellant's failure to comply with the condition the balance of the loan was to become immediately due and payable. Subsequently the oil company advised the appellant that so long as the mortgaged premises were used for the exclusive sale of its products no interest would be charged on the loan and that at the end of each month it would allow the appellant a credit of some $275 in reduction of principal until the entire debt was liquidated. In assessing the appellant for the years 1956 and 1957 the Minister included the monthly credits as income from the taxpayer's business. An appeal from the assessment was dismissed by the Tax Appeal Board. On a further appeal to this court the appellant contended that the credits in question constituted a forgiveness of debt and were capital receipts and not profits from a business.

Held: That whether the agreement between the appellant and Imperial Oil Ltd. be regarded as a conditional forgiveness of a debt secured by realty or a contract restricting the appellant's future trading rights, the monthly credits could not be considered to be profits from a business but were in the nature of capital receipts.

Commissioners of Inland Revenue v. *Coia.* 38 T.C., 334, applied.

St. John Dry Dock v. *M.N.R.* [1944] Ex. C.R. 186 and *Geo T. Davie and Sons Ltd.* v. *M.N.R.* [1954] Ex. C.R. 280, referred to.

APPEAL from a decision of the *Tax Appeal Board.*

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

Raymond Décary for appellant.

Paul Boivin, Q.C. and *Paul Olivier* for respondent.

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

DUMOULIN J. now (May 2, 1962) delivered the following judgment:

Il s'agit d'un appel interjeté d'une décision de la Commission d'appel de l'Impôt sur le revenu, datée le 18 août 1960[1], confirmant une cotisation du 10 décembre 1958, qui établissait une taxe de $87.18 sur le revenu de l'appelant pour l'année d'imposition 1956, et maintenait une autre cotisation, datée aussi le même jour, dans laquelle l'impôt réclamé, pour l'année 1957, s'élevait à la somme de $1,604.53.

[1] [1960] 25 Tax A.B.C. 65; 60 D.T.C. 476.

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GALIPEAU v. MINISTER OF NATIONAL REVENUE

Dumoulin J.

Les procédures devant la Commission de l'Impôt ont été versées au dossier de cet appel sous la cote A-4.

L'appelant, M. Edouard Galipeau, exerçait à Montréal, depuis 36 ans, en 1959, le métier de garagiste et de vendeur d'huiles lubrifiantes et d'essence motrice.

Par acte notarié, en date du 16 mars 1956, reçu devant Me Alain Voizard, notaire, Galipeau, afin d'agrandir son poste commercial, empruntait, de la compagnie Imperial Oil Ltd., $49,600 au taux d'intérêt annuel de 5 p. 100, comme il appert à la copie dudit acte produite sous la cote A-1.

Disons de suite que l'emprunteur, pour garantir le remboursement de cette somme, hypothéquait à la compagnie prêteuse, plusieurs lots ou parties de lots désignés au long dans l'acte authentique. L'on peut déjà conjecturer les clauses particulières et le but que se proposait l'Imperial Oil en consentant ce prêt: astreindre pendant une période de plusieurs années, 15 ans, un débitant fiable, exploitant un poste bien achalandé, à ne vendre que les produits de cette compagnie. Pareille intention est clairement exprimée à l'article V dudit acte, dont voici un extrait:

> . . . l'immeuble par les présentes hypothéqué sera exploité comme garage et/ou station-service pour la vente et le commerce (y compris l'achat et la vente) des produits pétroliers que IMPERIAL OIL LIMITED pourra offrir en vente aux détaillants et pour nulle autre fin et que l'emprunteur, ses successeurs ou ayants droit, achèteront de IMPERIAL OIL LIMITED et de nul autre tous les produits pétroliers dont le commerce (y compris l'achat et la vente) sera fait sur les lieux et dans l'immeuble ci-dessus mentionnés. *Pour les dits produits pétroliers l'emprunteur, ses successeurs ou ayants droit, paieront les prix ordinaires de vente de IMPERIAL OIL LIMITED aux détaillants en vigueur au moment de chaque achat.* (Les mots en italique sont à moi).

A défaut par l'emprunteur de respecter cette condition, le reliquat du prêt deviendra immédiatement exigible, sans excepter tout recours en dommages-intérêts auquel le prêteur aurait droit aux termes de cette convention.

Remarquons aussi que l'emprunteur, ou ses ayants droit, devront payer les prix réguliers fixés par la compagnie et ne bénéficieront d'aucun taux de faveur.

A l'article VI, l'emprunteur consent à la compagnie un droit de préemption du garage aux prix et conditions spécifiés dans toute offre faite de bonne foi, par une tierce partie.

L'article VII accorde aussi une option à la prêteuse de louer pour une période de 15 ans, à partir du 1er avril 1956, l'immeuble dont il s'agit, moyennant un loyer mensuel équivalant à $0.02 pour chaque gallon d'essence vendu dans le mois alors courant.

Ce long et prolixe document (pièce A-1) aurait pu, à toute fin pratique, être condensé dans les termes d'une contre-lettre échangée entre l'Imperial Oil et Edouard Galipeau, comprenant un extrait des minutes du Comité exécutif du bureau d'administration de la compagnie, daté le 29 mai 1956 (pièce A-2), et une lettre du 6 juin 1956 (pièce A-3), dont voici la teneur:

«*Pli recommandé*
Monsieur Edouard Galipeau
8644, rue St-Hubert
Montréal
Monsieur,

Nous reconnaissons par les présentes que, nonobstant les termes et conditions stipulés dans l'Acte d'Obligation consenti le 16e jour de mars 1956, par vous en notre faveur et passé devant Alain Voizard, notaire, il a été convenu entre nous comme suit:

Tant et aussi longtemps que l'immeuble hypothéqué avec garage et poste de service dessus érigés sera exploité pour la vente de produits pétroliers d'Imperial Oil Limited, et de nul autre, par vous, par un ou plusieurs de vos fils, par un ou plusieurs autres membres de votre famille ou par Imperial Oil Limited, ses représentants, ayants-droit ou sous-locataires aux termes de l'option de louer à icelle accordée par vous, conformément à l'article VII de l'Acte d'Obligation précité, aucun intérêt ne sera chargé sur ledit prêt de QUARANTE-NEUF MILLE SIX CENTS DOLLARS ($49,600) et, à la fin de chaque mois pendant lequel ladite propriété aura été ainsi exploitée, notre Compagnie vous donnera un crédit s'élevant à DEUX CENT SOIXANTE-QUINZE DOLLARS ET CINQUANTE-SIX CENTS ($275.56) en réduction du principal, de sorte que si lesdits garage et poste de service érigés sur ledit immeuble sont exploités comme tels pendant une période de CENT QUATRE VINGTS (180) mois, la dette de QUARANTE-NEUF MILLE SIX CENTS DOLLARS ($49,600) sera éteinte sans aucun paiement de votre part.

Pour votre renseignement, nous vous remettons, sous ce pli, une copie certifiée de la résolution adoptée par le comité exécutif de notre Compagnie le 29e jour de mai 1956, autorisant l'exécution de cette contre-lettre.

Bien à vous,
IMPERIAL OIL LIMITED
Le gérant des ventes

R. Laverdière/AP

signé R. Laverdière.»

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Dumoulin J.

Lors de l'audition de cet appel, les parties ont déposé au dossier une admission comportant que:

«L'appelant et l'intimé admettent par leurs procureurs soussignés que:

1. le montant emprunté par l'appelant servit entièrement à payer la construction et l'aménagement du garage et du service-station.

2. l'entreprise de l'appelant consiste en la vente des produits pétroliers d'Imperial Oil Ltd. et en la réparation de voitures.

Daté à MONTREAL, ce 20e jour du mois d'octobre 1961.

Raymond Décary
Procureur de l'appelant.

(Signé)

Paul Ollivier
Procureur de l'intimé».

Enfin, disons encore pour terminer l'exposé des faits, que le garage, objet de l'emprunt, fut bâti tel que promis et le montant de $49,600 versé à Galipeau dans une période de trois mois.

Les soumissions de droit formulées à l'appui de l'appel consistent à élaborer, sous diverses formes, l'idée maîtresse que l'emprunt, contracté pour la construction du garage, étant dès son origine une dépense d'établissement, un investissement de capitaux, l'éventuelle remise, selon les conditions prévues à la contre-lettre du 6 juin, conservait cette même qualité et ne participait aucunement du revenu de l'exploitation mercantile.

L'intimé, par contre, soutient que les articles 3, 4 et 139(1)(*e*) de la Loi de l'Impôt sur le revenu impriment le caractère de bénéfices commerciaux aux versements mensuels de $275.56 crédités à l'appelant selon les termes stipulés dans la contre-lettre du 6 juin.

La Cour doit donc trancher cette controverse et décider si les mensualités d'amortissement constituent une remise de dette, comme le voudrait l'appelant, ou des profits d'affaires selon les allégations de l'intimé.

A mon humble avis, les deux hypothèses qui précèdent n'en excluraient peut-être pas une troisième, qui serait de savoir si nous n'aurions pas ici tout simplement un contrat onéreux en fonction duquel l'Imperial Oil Ltd. obtiendrait d'Edouard Galipeau une sorte d'abdication de sa libre initiative commerciale. Comme nous l'avons vu, l'appelant se départit, quinze ans durant, du droit inhérent à tout négociant de conclure des arrangements d'affaires avec

d'autres que la firme précitée. Pour peu que cette interprétation soit admissible, l'on conviendra, je présume, qu'une pareille limitation de l'activité individuelle ne correspond guère à une «initiative ou affaire d'un caractère commercial», dont fait mention l'article 139(1)(*e*) de la Loi de l'Impôt sur le revenu (S.R.C. 1952, c. 148).

L'argument principal de l'un des procureurs de l'intimé est qu'une remise de dette ne saurait comporter ni restrictions ni conditions aucunes.

Telle est l'opinion qu'il émet à la page 31 de la pièce A-4 et je cite:

«Si cette remise était pure remise de dette sans autres conditions et sans autres considérations, je dirais, me rangeant avec la Cour d'Échiquier dans la cause de Davie, que mon confrère a citée, je dirais que ces paiements ou remises en acompte de capital ne sont pas du revenu ...»

Pareil avis me semble excessif et outrepasser les habitudes du commerce où de telles ententes sont d'ordinaire conditionnelles. En d'autres termes, la spécification statutaire d'un abandon de dette dépend moins de ses modalités d'extinction que de la nature même de la créance originelle.

A la page 34 du dossier des procédures (A-4), le procureur de l'intimé se réfère à M. le Juge Abbott, de la Cour suprême du Canada, dans la cause d'*Oxford Motors Ltd. v. The Minister of National Revenue*[1]. L'honorable Juge écrivait alors que:

The British Mexican case did not decide, that under no circumstances can the forgiveness of a trade debt be taken into account, in determining the taxable profit arising from the carrying on of a business, and I have found no subsequent case in which it has been so held. No one has ever been able to define income in terms sufficiently concrete to be of value for taxation purposes. In deciding upon the meaning of income, the Courts are faced with practical considerations which do not concern the pure theorist seeking to arrive at some definition of that term, and where it has to be ascertained for taxation purposes, whether a gain is to be classified as an income gain or a capital gain, the determination of that question must depend in large measure upon the particular facts of the particular case.

Si je ne m'abuse, ces lignes n'infirment point ce que je viens d'avancer.

[1] [1959] S.C.R. 548-553.

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Aux pages 34 et 35, l'intimé voudrait s'autoriser de cette comparaison:

> Ainsi, si je prends $200 à même mon salaire pour acquitter mes versements d'hypothèque sur ma propriété, j'acquitte certainement une dette de capital; il n'y a pas d'erreur. Mais mon deux cents dollars n'en reste pas moins du salaire, du revenu, et il me faudra l'inclure dans mon revenu de la fin de l'année.

Excellent exemple pour autant, mais mauvais argument en l'espèce. Que l'on établisse où et quand, l'appelant «prend $275.56 à même son salaire pour acquitter ses versements d'hypothèque sur sa propriété», et alors, mais alors seulement, je reconnaîtrai une analogie valable entre ce rapprochement extrinsèque et le fait réel. Dans l'évolution normale de notre cas, la compagnie Imperial Oil, à l'expiration des 180 mois, aura éteint d'elle-même sa réclamation hypothécaire contre Edouard Galipeau.

L'appelant ou ses successeurs légaux devront, en effet, pendant 15 ans, acheter exclusivement les marchandises de la compagnie prêteuse, sinon la remise de dette cesserait automatiquement. Que l'on me passe cette lapalissade de dire que ce n'est pas l'achat, mais la revente à profit qui crée l'enrichissement. Or, il est raisonnable d'appréhender que M. Galipeau, chemin faisant, devra refuser, de la part de quelques compétitrices de l'Imperial Oil, l'offre de conditions préférables, s'il entend bénéficier de son contrat antérieur.

Je ne puis accueillir davantage l'intention d'assimiler cette extinction graduelle d'une dette immobilière à un escompte proportionnel au chiffre de la vente, selon les termes de l'un des avocats du Ministre: «Vends mes produits. Si tu fais bien ça, je te donnerai $1,000 par année.» Nous avons vu qu'il n'existe dans le contrat de prêt aucun rapport de cause à effet, si je puis dire ainsi, entre le rythme du débit des produits de l'Imperial Oil et la diminution mensuelle du solde de l'emprunt, mais, seule, l'unique obligation de ne pas vendre des huiles lubrifiantes ou de l'essence motrice achetées ailleurs que chez la compagnie précitée.

Dans le cas des manufacturiers anglais, Nuffield et de leur cliente, l'Oxford Motors, une véritable prime de vente lui fut consentie, soit une réduction de $250 pour chaque automobile vendue par la firme canadienne. On le conçoit, cet allégement s'effectuait en raison directe des unités vendues et demeurait inopérant si aucune vente n'intervenait.

Les procureurs des deux parties ont déclaré qu'aucun litige du genre n'avait encore été soumis à la Cour de l'Échiquier du Canada. Par ailleurs, l'appelant a fait valoir un précédent écossais, de récente date, 1959, et qui me semble avoir une ressemblance presque photographique à notre cause. Il s'agissait de l'instance: «*Commissioners of Inland Revenue v. Coia*[1]», où la question de principe à trancher, analogue à celle qui se pose ici, fut déférée en appel à la première division de la «Court of Session» d'Écosse, siégeant comme Cour de l'Échiquier. Voici les données essentielles de cette cause:

In 1951 the Respondent, a garage proprietor, entered into an agreement with a petrol company whereby the company undertook to contribute towards the cost of purchasing additional ground and building extensions to his garage and workshops, and, in return, the Respondent agreed to take all his requirements of motor fuels exclusively from the company for ten years. The sums to which the Respondent became entitled under the agreement were based on his past and estimated future sales of petrol as well as on the amount spent on the extension and improvement of his premises.

An additional assessment to Income Tax for the year 1952-53 was made upon the Respondent in respect of sums received under the agreement, on the footing that these sums were profits of his business as garage proprietor. On appeal, he contended that the sums, being received only in reimbursement of capital expenditure incurred and as lump sums in consideration for accepting a restriction in future trading rights, were in the nature of capital receipts. The General Commissioners upheld this contention and allowed the appeal.

Held, that the sums received were of a capital nature.

Le lord President (Clyde), analysant l'essentiel de l'entente, dégagea comme l'un de ces facteurs déterminants celui-ci:

From the language of the agreement it appears to me quite clear that the Respondent got a money payment for a capital expenditure by him as the consideration for his giving up his freedom of trading and changing the structure of this part of his business so as to make it in effect an agency for the sale of the Esso Petroleum Co.'s fuels. The Esso Company were willing to pay £1,100 for the securing of this benefit over a period of ten years. That in itself would in the circumstances of this particular agreement be enough to lead to the inference that the moneys paid to reimburse this capital expenditure were of a capital nature.

Lord Patrick, un autre des juges de la Cour de l'Échiquier écossaise, exprima le même avis, en ces termes:

In return he parted with what I regard as a valuable asset of a capital nature, the right to obtain the supplies of fuel oils which were his stock-in-trade from such sources as he might consider most suited to the varying

[1] (1959) 38 T.C. 334.

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nature of the demands made by his customers, and the right to obtain these fuels in the cheapest market. For ten years he must buy his supplies of motor fuels from the Esso Company, and he must buy them at such prices as the Esso Company chose to exact. It seems to me that a sum of money which a trader receives to enable him to obtain valuable assets of a capital nature, a sum which he can only obtain if he does so add to his capital assets, and in return for which he parts with a valuable asset of a capital nature, cannot properly be described as a trading profit.

A mon sens, quelle que soit l'optique selon laquelle on entrevoit la convention à l'origine de ce litige, remise conditionnelle de dette immobilière ou contrat limitatif de la liberté d'action du promettant, ni l'une ni l'autre de ces suppositions ne possèdent les caractéristiques «d'une initiative ou affaire commerciale» que prétendrait lui attribuer l'intimé en fonction, toujours, des articles 3 et 4 de la loi fiscale.

J'ajouterai que deux autres décisions de notre Cour, longuement commentées par les contestants, celles de *St. John Drydock v. The Minister of National Revenue*[1] *et George T. Davie and Sons v. The Minister of National Revenue*[2] servent à me confirmer dans l'opinion que j'adopte.

Pour les motifs précédemment formulés, je crois devoir infirmer la décision de la Commission d'appel de l'Impôt, et maintenir le présent appel, avec dépens.

Le dossier de la cause sera retourné au Ministre intéressé afin que soit faite une nouvelle cotisation conforme à ce jugement.

Jugement conforme.

[1] [1944] Ex. C.R. 186. [2] [1954] Ex. C.R. 280.

BETWEEN:

THE SHIP *ARGYLL* AND HER OWNERS, (Defendants and Counter-Claimants) ..... APPELLANTS;

AND

THE OWNER OF THE SHIP *SUNIMA*, AKSJE SELSKAP I.M.A. (Plaintiff) . RESPONDENT.

1961
March 23, 24
1962
May 2

Shipping—Collision in Quebec City Harbour—Negligence of defendant ship sole cause of collision—Contravention of Rules 29, 25 and 22 of the International Rules of the Road—Appeal dismissed.

Respondent recovered judgment against the appellants for damages resulting from a collision between its vessel and that of the appellants. From that judgment the defendants now appeal to this Court.

Held: That on the facts as found by the learned trial Judge the appeal must be dismissed.

2. That the collision and resulting damage were caused solely by the negligence and fault of those in charge of appellant ship in contravening rules 29, 25 and 22 of the *International Rules of the Road* in that they failed to keep to the side of the fairway or mid-channel which lay on their starboard side, in failing to post a look-out on the bow of the vessel and in altering the course of their vessel to port which brought her on a course which crossed that of plaintiff vessel.

3. That this court sitting in appeal in admiralty matters will not interfere with the judgment of the lower court as regards pure questions of fact or the quantum of damages unless it appears clearly erroneous. The S.S. *Ethel Q v. Adelard Beaudette*, 17 Ex. C.R. 505 applied.

APPEAL from the judgment of the District Court in Admiralty for the Quebec Admiralty District.

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

Jean Brisset, Q.C. and *Bruno Desjardins* for appellants.

R.C. Holden, Q.C. and *A. S. Hyndman* for respondent.

DUMOULIN J. now (May 2, 1962) delivered the following judgment:

This is an appeal from a decision rendered June 29, 1960, by Honourable Justice Arthur I. Smith, District Judge for the Admirality District of Quebec, maintaining the Plaintiff's action and, consequently, dismissing the Defendants and Counter-Claimants' pleas.

1962

THE SHIP *Argyll* v. THE SHIP *Sunima*

Dumoulin J.

The maritime mishap, from which stems the instant suit, happened between 0200 and 0205 or 0206 hours, the night of May 27, 1959, within the limits of Quebec City harbour.

Weather conditions were excellent, a clear, starry night, no wind, a calm sea. An ebb tide was flowing east at an approximate velocity of 3 to 3½ knots.

Despite these favourable climatic factors, a serious collision occurred causing considerable damage to both ships when they rammed one another in the circumstances hereunder narrated.

The vessels concerned, the *Sunima* and *Argyll*, can be described as having respectively:

The *Sunima*: an overall length of 354.95 feet, a breadth of 48.65 feet; 3,903.06 tons gross, 2,118.97 tons net register, and manned by a crew of 34. At full speed, loaded, she could develop 14¼ knots, hourly.

Of Norwegian registry and build (1958), the *Sunima* is a steel, single screw, diesel cargo motor ship, with a draught of 9'9" forward and 15'10" aft. Her bridge is located amidships and her housing quarters aft.

The *Argyll*, built in Japan in 1957, has an overall length of 504 feet, a breadth of sixty-two feet six inches (62'6"), a gross tonnage of 10,657 and a net register of 6,304 tons. She attains, at full speed, 15 knots, and 11 at half speed on 60 R.P.M. This ship, an oil burning one, has a single right-hand propeller; her draught, if travelling light, as on this ill-fated trip, reads 6'6" forward, and 19'6" aft. Her wheelhouse is located 366' aft of the stem. Of Liberian registry (Port of Monrovia), the *Argyll*, on May 27, 1959, had a Greek crew of 37 men.

The *Sunima's* Master was Captain Sverre Swertsen, the *Argyll's* Captain, Antonios Corcodilos. Pilot Moise Dionne navigated the *Sunima* and Pilot E. Gourdeau the *Argyll*.

At the material time, the *Sunima*, laden with 741 tons general cargo, had begun a voyage from Montreal to the British West Indies, whilst the *Argyll* made way, in ballast, from Port Alfred to Sorel, P.Q.; the plaintiff ship, therefore, going down river, in an out-bound direction, and defendant vessel steering an in-bound upstream course.

In a general way, it may be said that the collision took place about two miles (nautical) below Quebec City pilotage station, but of this more will be written.

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Possibly not the most concise mode, but I believe, a helpful and revealing one, of setting forth the flatly divergent explanations resorted to by the contending parties, will consist in textually inserting paragraph 12 and, partially paragraph 16 of the Combined Preliminary Acts.

In paragraph 12, then the *Sunima's* version is that:

She was on a voyage to the British West Indies, via Halifax, N.S. As the *Sunima* approached the Pilotage Station in the Harbour of Quebec her engines were stopped and her way reduced. After changing pilots, the *Sunima* proceeded on down the channel on the usual outward bound course. When about opposite the entrance to the St. Charles River Basin and in about mid-channel the red side light and masthead lights of an upbound ship (which turned out to be the *Argyll*) were sighted about two points on *Sunima's* starboard bow and distant about 1½ to 2 miles. *Sunima* was altering course gradually to starboard and expected to meet and pass the *Argyll* port to port in the usual manner but shortly afterwards it was noticed that the *Argyll* appeared to be altering her course to port, opening her green light and closing her red.

The course of *Sunima* was altered further to starboard and a signal of one short blast was sounded by her. The *Argyll* did not reply and continued to swing to port evidently intending to cross ahead of *Sunima*. The engines of *Sunima* were put full speed astern and her wheel hard to starboard and an attention signal of several short and rapid blasts was sounded, but the *Argyll* came on, crossing in front of *Sunima* and making collision inevitable.

Next, the *Argyll's* plea reads thus:—

The *Argyll* had been proceeding upriver with her engines turning at full speed and her telegraph on stand-by; upon entering the limits of the Harbour of Quebec, her speed was reduced to half.

After sighting the lights of the *Sunima*, the *Argyll* kept her course and speed, keeping well on her own side or north side of the channel and expecting to meet the *Sunima* which was down-bound, red to red; about 4 cables above Buoy 87½B the course of the *Argyll* was altered to 250° True, in order to make the bend in the channel leading into the dock area of the Harbour of Quebec, bringing Buoy 138B to bear fine on the starboard bow; the green light of the *Sunima* which was then bearing fine on the port bow of the *Argyll* was kept under close observation as those on board the *Argyll*, expected her at any moment to alter course to starboard in order to effect a port to port meeting; the *Sunima*, however, kept on showing her green, shaping to be on a course crossing that of the *Argyll* from port to starboard at very close quarters, whereupon it became apparent that a collision would be unavoidable unless action was taken by the *Argyll*; the wheel of the *Argyll* thereupon was ordered hard-a-port and a signal of 2 short blasts blown and the *Argyll* began to swing to port; simultaneously, the *Sunima* was seen to alter her course sharply to starboard closing her green and opening her red on the starboard bow of the *Argyll*, and the collision occurred after which the engines of the *Argyll* were stopped; by reason of the impact, the swing of the *Argyll's* bow to port was accentuated and the *Sunima* continued to swing to starboard until both vessels came to head south; various manoeuvres being made until both vessels were clear.

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The point of impact can be fairly well located, the weight of evidence lending reasonable probability to Pilot Dionne's reckoning who indicated it by letter "D" on chart 1321 (Plaintiff's ex. P-1), and on page 28 of the transcript is reported to have said that:

> A. It happened in between the two (2) dry docks, just at the end of the outfitting dock there . . . . It would be between the Lorne and the Champlain dry docks, a little to the east of the outfitting dock.

Such an estimation disagrees with the marking "G", pencilled in red on the same map, as giving Pilot Gourdeau's and Captain Corcodilos' versions, situating the critical spot well to the north of mid-channel. This suggestion is inadmissible for several reasons, the first of which shows through appellants' paragraph 12 of the Combined Preliminary Acts. The *Argyll's* emergency step is therein given as "hard-a-port" order, with the subsequent recognition that "both vessels came to head south" manifestly implying south of mid-channel and in *Sunima's* starboard lane.

On this significant point I share the learned trial Judge's opinion that:

> There is no evidence to show that the *Sunima* was at any time to the North of mid-channel save and except for the calculations made by the *Argyll's* Pilot and Master as to the place of the collision.
>
> The testimony of these witnesses however on this point is confused and, in particular, that of Pilot Gourdeau appears to have completely disregarded and failed to take into account the *Argyll's* alteration from course 270 to 250 and the fact that the *Argyll* was undoubtedly on course 250 for upwards of two minutes prior to her going hard-a-port just prior to the collision.

The position of impact suggested by Pilot Dionne differs somewhat from that found by the Court below, and would be about 4 cables beyond Buoy 87½B; however, I quite agree with my assessors that it had no material bearing on the actual cause of the collision.

According to the indications jotted down on chart 1321, i.e., the letters "S" and "A", Pilot Dionne, who testified to this, sighted the *Argyll's* red side lights and masthead lights when his own ship stood opposite the entrance to the St. Charles River Basin, a stretch of roughly two (2) miles separating the vessels (cf. Dionne, p. 17). On the other hand, the *Argyll's* Master, Antonios Corcodilos (cf. his evidence, pp. 27-28), perceived the down-bound *Sunima* a few

minutes later, at 0203, when Pilot Gourdeau rang a half speed signal preparatory to altering the course from 270° to 250°, as required by a rather sharp bend in the channel.

Now, this variation, which swung the in-bound *Argyll* to port, towards the *Sunima*, must, if imprudently made, bear a heavy burden of responsibility as a proximate cause in the genesis of the accident, especially so since its critical phase evolved within, probably, no more than two minutes, from 0203 to 0205. Athanasios Klendos, the *Argyll's* Chief Engineer, reported that as closely as he could figure, the impact occurred at 0205, "because at that time it is between two movements", very likely those of half speed and hard-a-port (p. 133). In line with the verbal indication of 0205 is the mute evidence of appellants exhibit A, the Chief Officer's log book, registering under date of May 27, 1959, a gyro course of 270° at 0200, continuing until 0205, when the reading is 250°.

Constantinos Valmas, Second Officer on the *Argyll*, corroborates Klendos as to the time, 0203, at which a half speed order was rung.

In Valmas' evidence some assertions sound unconvincing. For instance he says the *Sunima* was 2 or 3 cables distant when he last saw her prior to the collision, and that her green and masthead lights were open to the *Argyll's* port side (trans. p. 154). He then descended below deck and, less than two minutes later, when the tremendous shock took place, no possibility of a collision came to his mind, but this only and I quote (p. 157):

A. I thought that the ship was aground and that is all.
Q. by Mr. Brisset, Q.C. Why did you think the ship was aground?
A. Because we had passed very near the West Point Light.
Q. Where did you think the other ship was? You did not think there was a collision with the other ship?
A. No.
Q. Where did you think the other ship was?
A. That she was far away.
Q. Where did you think the other ship was?
A. Far to the port side, I thought.

Whatever credence this testimony might deserve the fact persists that Second Officer Valmas positively felt the course steered by the *Sunima*, a few score seconds before the mishap, offered no danger because the latter "was far to the port side". If this be better than guesswork, what then did

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bring the vessels in immediate contact? Manifestly a false move; but on whose part? Such is the moot point the Court must solve.

The respondent's story, if I be permitted this expression, is coherently related in a precise, unvacillating manner by Pilot Dionne, who sighted the in-bound *Argyll* two miles off, abeam Ste. Petronille light, showing her 2 masthead lights and her red ones. Dionne had set a course of 070, which he increased to 080 on perceiving the other ship's "red and green side lights and the two (2) mast lights almost in line or practically in line . . . and at the same time watching the *Argyll*" (Trans. pp. 17-18). As the on-coming steamer passed abeam of Buoy 87½B, continues Dionne, "with all her lights in line toward me", there lay an intervening space of roughly three quarters of a mile (p. 19). The *Sunima's* wheel was turned to starboard on an 080° run. From there on, Dionne could not understand the unusual route on which the other boat kept going and he next saw her green lights as both ships came very close (p. 20). He ordered another five (5) degrees, and a few seconds later, one short warning blast and hard to starboard. Nonetheless, the *Argyll* "seemed to go more to port; so then I gave the order to stop the ship and to go astern; but by then the two (2) ships were pretty close together", pursues Pilot Dionne, who finally states that the *Argyll* headed across the *Sunima's* way at an angle of two or three points, with the dire consequence that the *Sunima's* stem hit the other vessel's starboard bow 20 or 25 feet abaft her stem. (cf. exhibits P-8 (a & b), P-9 (a & b), and pp. 21-22).

On appellants' behalf the Master, Captain Antonios Corcodilos, and Pilot Ernest Gourdeau, of Quebec City, testified at great length. A diligent sifting of their evidence leaves me skeptical, and under a persistent impression that in some measure, on crucial points, it results from afterthought or even wishful thinking.

The Court does not alone entertain a somewhat dubious opinion. For motives different, doubtless, but verging towards comparable results, the appellants' learned counsel could not compile a 57 page "Synopsis of Argument" without incurring the annoyance of taking polite yet firm exception to some important parts of the evidence adduced by his four principal witnesses, the Captain, the Pilot, the Chief Engineer and the Engineer of the Watch.

Starting on page 36 of this written submission, we find Pilot Gourdeau reproached thus:

> Pilot Gourdeau in his evidence in chief evidently made a mistake at Page 164 of the Transcript of the Evidence at the trial, when he stated her course (i.e. the *Sunima's*) as being 020°T. to 025°T. He later corrected that to in between 045°T. and 055°T. at P. 207.

I may remark that this so-called correction on pages 207 and 208 does wear a conjectural appearance.

On page 38 of the Synopsis, Gourdeau is blamed for his inaccuracy in stating that the Sunima was bearing about 3 points on the *Argyll's* port bow.

Lower, on the same page (38), we read that:

> In the *Argyll's* Preliminary Act, it is alleged that such change of course took place 4 cables above Buoy 87½B, while in her Statement of Claim, it is alleged that this change took place between 3 and 4 cables above Buoy 87½B.
>
> The evidence of Captain Corcodilos (Trans. *Argyll*, P. 32) is to the effect that the change of course was made 4 cables past Buoy 87½B.
>
> Pilot Gourdeau in his evidence (Trans. Trial, P. 165), gave this distance as being 5 cables past Buoy 87½B. He stated, however, that the green light on the Outfitting Wharf of Lorne Drydock was bearing 60° on his port side when he made the change, this being his usual mark; *however, according to our plotting,* this places the *Argyll* more like 4 cables above Buoy 87½B (the emphasis is not in the text).

In a wide expanse of river those discrepancies would be of slight moment, but in the restricted harbour lanes within which the collision happened, a matter of two cables more or less, 1,200 feet, spells the difference between safety and disaster. Furthermore, must we deal with three separate course plotters, the Master, the Pilot and some eerie helmsman, anonymously hinted at by the expression "according to our plotting"?

More indicative, still, of the many inconsistencies alluded to above, are Mr. Brisset's criticisms aimed at certain statements of the Engineer of the Watch, Valmas, and Chief Engineer Klendos. I deem appropriate to reproduce the whole paragraph from page 40 of the Appellants' Synopsis of Argument:

> The only witness on the *Argyll* who gave 0205 as the time of the collision was the Engineer of the Watch, but in this he is contradicted, and we submit that he was in error; in any event, he contradicted himself by stating that the collision occurred one minute before he received the stop order which he recorded as having been rung at 0208. The Chief Engineer, it must be conceded, had recorded in his own Log Book that the collision had occurred at 0205 but it seems that this was an estimate on his part, which might have been based on a hasty consideration of the actual events, but evidently, having made the entry,

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the Chief Engineer was committed although he conceded that the time was purely an estimate and that the time he entered would not necessarily be as accurate as the time of an order received from the bridge. The estimate in any event was made only after the collision (Trans. *Argyll*, P. 33, 34 & 35). The engine of the *Argyll* was not stopped until 0208 which, if the collision occurred at 0205, would mean that it was kept turning at half speed ahead for 3 minutes after the collision. This is hardly likely and much more probable that the engine was stopped not long after the collision and that therefore the collision occurred at 0207 rather than at 0205.

If the preceding analysis of the reliance attaching to such a style of hypothetical and *ex post facto* evidence, should extend from the learned counsel's mind to my own, I could, possibly, feel warranted, to dismiss the appeal without further ado. I will, however, persist in disposing of the remaining angles of the case.

My attention was also attracted by certain answers of Captain Corcodilos in reply to his principals' lawyer. The excerpts hereunder are taken from pages 36, 37 and 38 of the transcript.

By Mr. Brisset:

Q. Now, we would like you to tell us in your own words what happened after that?

A. Yes. I saw that the ship (*Sunima*) was not changing her course, a thing that we thought he ought to do before that. Then I saw her very close, the distance was getting smaller and there was danger of a collision as we were going. It was about a cable (600') or something like that so I decided the only manoeuvre I could do was to put the wheel hard to port to pass—to port to pass green to green, because we were very close. Also at the same time the pilot gave the ORDER "Hard to port".

Next, ten lines down, on page 37 of the transcript, a suggestive question is put to Captain Corcodilos in examination in chief; I quote:

Q. Now, in what direction was she heading in relation to your bows? Was she (*Sunima*) crossing your bows in one way or another?

A. She was crossing our head.

Q. In what direction?

A. From port to starboard.

* * *

Q. Now, Captain, at that stage would it have been possible for you to go to starboard?

A. No.

Q. Why?

A. First there was very close the shallow water to the north. The river is very shallow water here.

As one might expect, those leading questions met with due compliance, though not dispelling all doubts regarding the feasibility for the *Sunima* to keep on her course, ("was not changing her course", has just said Corcodilos), and, simultaneously, be crossing the *Argyll's* stem "from port to starboard".

The alleged proximity of shallow water to the *Argyll's* starboard at point "G", marked by Corcodilos and Pilot Gourdeau on plaintiff-respondent's exhibit P-1 (official chart no. 1321), reveals, on the Master's part, sailing up-river for the second time only, his ignorance of the soundings reported on that map; the depth, thereabouts, ranging from 121 to 128 feet. The Beauport shoreline, in a north-easterly direction, with an outer depth of 40 feet, lies about 4 cables to the right of point "G", surely affording sufficient room for a swing to starboard of a vessel with a forward draft of 6'6" and an aft one of 19'6".

A last instance of conflicting testimonies will finalize this chapter. Pilot Gourdeau, on examination by defendant-appellant's counsel, is asked (transcript p. 171, top line):

> Q. Now, how far off was she (the *Sunima*) when you altered course from two seven oh (270) to two five oh (250)?
>
> A. She was about a mile and one-quarter (1-¼) above me.

Oddly enough, the *Argyll's* Master, who at the time stood "in the wheelhouse, close to the pilot" (trans. p. 33), answers, to this selfsame question, that the other ship was then distant: "About three (3) cables" (trans. p. 33, bottom line). Quite a gap indeed between a mile and one quarter, or 6,600', and three (3) cables, or 1,800', on the part of two trained seamen, had their attention been really focussed upon an identical object.

SPEED—

The appellants' statement of defence and counterclaim at paragraph 14, affirms that:

> The *Sunima* was proceeding at an excessive and immoderate rate of speed in contravention of the Regulations of the National Harbours Board in force in the Harbour of Quebec;

Operating regulations of the National Harbours Board, Order in Council (P.C. 1954-1981), dated December 16, 1954, section 35(1) enacts that:

> 35(1) No vessel shall move in the harbour at a speed that may endanger life or property

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(2) without restricting the generality of subsection (1) no vessel shall move at a rate of speed exceeding
at Quebec—nine knots.

Apparently, these cautioning directions were disregarded by Pilot Dionne, and the learned trial Judge was so advised by his assessors. I also had the assistance of experienced seamen in whose estimation the *Sunima* proceeded at a speed of 18 knots over the ground. Pilot Dionne at page 112 of his evidence suggests the reason for such regulations. Explanations are, of course, predicated on their respective degree of plausibility, but, at all events, it seems worthwhile to relate this one at length.

Dionne, asked by cross-examining counsel:

. . . Pilot, do you not agree that a speed of this kind makes it very easy to miss the turn when the turn has to be made?

replies:

No, sir. The speed of a ship at Quebec—the regulation is made for ships alongside the wharfs here, so as not to make too much sea, too much waves. It is not for the waves that regulation is made but it is made for the ships that are alongside the wharf. And that night there were no ships at Quebec, there, and the weather was very clear and calm (trans. p. 112)

Irrespective of Dionne's interpretation, this is not a penal action for infringement of speed regulations, and this derogation concerns the Court insofar only as the evidence indicates it was a proximate cause of the accident.

The Court below deleted speed as a contributing element, and nothing in the record perused would justify me to hold differently.

LACK OF PROPER WATCH ON THE ARGYLL—

The learned trial Judge, at page 8, last paragraph, writes:

Those on board the *Argyll* were, moreover, guilty of fault and negligence in failing to post a lookout on the bow of the vessel having regard to the admitted difficulty of distinguishing ships' lights against the back-ground of the lights of Quebec City and harbour front. I have no doubt that the failure to post a lookout contributed to the bringing about of the collision, since I am convinced that the *Sunima* was not sighted by those in charge of the *Argyll* as soon as she should have been.

I fully agree with the tenor of this finding, both as to the poor seamanship and grave imprudence of omitting the regular look-out and watch precautions, especially at night, within frequented harbour lanes, and also as to the confusing glare of city lights shimmering on the glossy surface of calm waters.

The *Argyll*, a bulk dry cargo vessel, 504 feet overall length, has her bridge and wheelhouse aft, a peculiarity which, presumably, does not detract from the urgency of posting the usual look-out.

Nonetheless, Captain Corcodilos, at pages 75, 100 and 101, admits that the look-out and second officer went down, two or three minutes before the collision, to inspect the port and pilot ladders.

Some seconds before the impact, Captain Corcodilos, new to St. Lawrence sailing intricacies, and Pilot Gourdeau, busy with the ship's navigation, stood alone on the aft deck. This unusual state of affairs is conceded in the Appellants' Synopsis, and an attempt had at brushing it aside as of slight consequence, since, so the allegation goes, watch or no watch, look-out or no look-out, the accident would have taken place just the same; an assumption presupposing, at best, a brimful measure of surmising.

Sighting the *Argyll*, the *Sunima* could expect the former had also located her, as normally she should have, and would not resort to an unpredictable alteration from 270° to 250°, plus a further deviation hard to port, thereby rendering the collision unescapable.

As for so sudden a change of course, my assessors believe it happened "prematurely, and had (the *Argyll*) continued on 270 degrees for a little longer time, the risk of collision would not have existed and both vessels would have passed safely port to port". The preponderance of evidence favours this opinion. And the origin of all errors attributable to the *Argyll's* navigators springs from a lack of diligent surveillance.

The pertinent jurisprudence, of which two instances follow, insists on the urgent need of having continuous and properly posted look-outs.

In Re: *The Silver City*[1], Mr. Justice Higgins, sitting in the Supreme Court of Newfoundland, (in Admiralty) wrote:

> . . . To constitute a good look-out on a ship there must be a sufficient number of persons stationed for the purpose, who must know and be able to discharge that duty. The look-out should not have any other duty to perform (*The Glannibanta*, 1 P.D. 283). *The officer of the watch or the man at the wheel does not satisfy the requirements as to look-out* (the *Hibernia*, (1874) 2 Asp. 454. (Emphasis is mine).

[1] (1935) 51 Lloyd's List L.R. 135 at 143.

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and Mr. Justice Willner (The Admiralty Division), in Re: *The Dea Massella*[1] spoke to this effect:

> . . . Having prefaced what I have to say with those remarks, I do want to go on to say that I am not satisfied as to the look-out which was kept on board either of these vessels. *In particular, I am not satisfied with the fact that both vessels sought to station their look-out men on the bridge, the navigating bridge.* That is a matter on which I have already, in previous cases, on the advice of the Elder Brethren, commented adversely; and I thought it right to ask the Elder Brethren who are advising me in this case what is their view of the practice of stationing the look-out man on the navigating bridge. They, like other Elder Brethren who have previously advised me, again condemn that as bad practice. *They tell me that the look-out should certainly be stationed somewhere else in the ship; forward, if possible, if the weather conditions allow it. If, however, the weather is such as to forbid the possibility of a look-out being posted forward, then at least he ought to be stationed on the upper bridge. They express the view, which I think I have already included in my judgment in previous cases in this Court, that it is most important to station the look-out in a position where his attention will not be distracted by what is going on on the bridge, where he will not be perpetually listening to discussions taking place between the master and the officer of the watch, or between the officer of the watch and the helmsman, but where he can give his undivided attention to what he is himself able to see and hear . . .*

Lastly, there exists little room for doubt but that Appellants' officers contravened the *International Rules of the Road,* particularly articles 29, 25 and 22, hereafter cited according to their chronological sequence of occurrence.

Article 29: Nothing in these rules shall exonerate any vessel, or the owner, or master, or crew thereof, from the consequences of any neglect to carry lights or signals, or of any neglect to keep a proper look-out or of the neglect of any precaution which may be required by the ordinary practice of seamen, or by the special circumstances of the case.

Article 25: In narrow channels every steam vessel shall, when it is safe and practicable keep to that side of the fairway or mid-channel which lies on the starboard side of such vessel.

Article 22: Every vessel which is directed by these rules to keep out of the way of another vessel shall, if the circumstances of the case admit, avoid crossing ahead of the other.

For an ultimate summing up of my findings in this appeal, I could do no better than adhere to the learned trial Judge's conclusions who then wrote:

> I am satisfied that the casualty was brought about solely by the fault and negligence of those in charge of the *Argyll,* in that they improperly failed to keep to the side of the fairway or mid-channel which lay on their starboard side and instead of altering course to starboard,

[1] [1958] 1 Lloyd's Rep. 10 at 21.

as they could and should have done when the *Sunima* was sighted, they altered to port in a manner which brought the *Argyll* on a course which crossed that of the *Sunima*.

Those on board the *Argyll* were, moreover, guilty of fault and negligence in failing to post a lookout on the bow of the vessel having regard to the admitted difficulty of distinguishing ships' lights against the back-ground of the lights of Quebec City and harbour front. I have no doubt that the failure to post a lookout contributed to the bringing about of the collision, since I am convinced that the *Sunima* was not sighted by those in charge of the *Argyll* as soon as she should have been.

Finally, *ex majore cautela,* merely, and nowise restricting my full concurrence with the above pronouncement, the doctrine applicable in an appeal such as the instant one, was adequately formulated by the late Mr. Justice Audette in the matter of *The S.S. Ethel Q v. Adélard Beaudette*[1], I quote:

> Sitting as a single judge in an Admiralty Appeal from the judgment of a trial judge, while I might feel obliged to differ with great respect in matters of law and practice, yet as regards pure questions of fact or the quantum of damages, I would not be disposed to interfere with the judgment below, unless I came to the conclusion that it was clearly erroneous.

For the reasons preceding, this appeal and the corollary counter-claim are dismissed. The respondents will recover the costs incurred in both this Court and that below.

Judgment accordingly.

Reasons for judgment of A. I. Smith, D.J.A.:—

This litigation, comprising Principal Action and Counter-Claim, arises out of a collision which occurred between the Ships *Sunima* and *Argyll* within the limits of the Harbour of Quebec at approximately 0205 hours (E.S.T.) on May 27, 1959.

The case for the plaintiff is as follows:— The plaintiff is and was at the time of the collision hereinafter referred to, the owner of the Norwegian motor-vessel *Sunima*, a steel single screw cargo vessel of the Port of Oslo, Norway, of 3,903.06 tons gross and 2,118.97 tons net register, 354.05 feet in length overall and 48.65 feet in breadth and manned by a crew of 34 all told. On May 27, 1959 the *Sunima*, laden with about 741 tons general cargo was on a voyage from Montreal to the British West Indies. The weather was clear with good visibility and there was little or no wind. The tide was ebb of a force of about 2 knots. The *Sunima* was exhibiting the regulation navigating lights which were burning brightly and a good lookout was being kept on board her. Early in the morning of the said May 27 the *Sunima*, when approaching the Pilotage Station in the Harbour of Quebec, reduced her speed and then stopped her engines, taking off her way in order to

[1] 17 Can. Ex. C.R. 505 at 506.

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change pilots. After changing pilots, the *Sunima* proceeded on down the channel on the usual outward bound course. When about opposite the entrance to the St. Charles River Basin and in about mid-channel the red light and masthead lights of an upbound ship (which turned out to be the *Argyll*) were sighted about two points on *Sunima's* starboard bow and distance about 1½ to 2 miles. *Sunima* was altering course gradually to starboard and expected to meet and pass the *Argyll* port-to-port in the usual manner but shortly afterwards it was noticed that the *Argyll* appeared to be altering her course to port, opening her green light and closing her red. The course of *Sunima* was altered further to starboard and a signal of one short blast was sounded by her. The *Argyll* did not reply and continued to swing to port evidently intending to cross ahead of *Sunima*. The engines of *Sunima* were put full speed astern and her wheel hard to starboard and an attention signal of several short and rapid blasts were sounded, but the *Argyll* came on, crossing in front of *Sunima* from port to starboard. The collision then occurred, the starboard bow of *Argyll* a short distance abaft her stem striking the stem of *Sunima*, causing serious damage to the *Sunima*. The collision and the damage occasioned to the *Sunima* were caused by the fault and negligence of the *Argyll* and those on board her as herein alleged. Those on board the *Argyll* improperly failed to keep to the side of the fairway or mid-channel which lay on their own starboard side. They failed to alter their course to starboard in due time or sufficiently or at all. They improperly altered their course to port. They negligently failed to keep a good lookout. They proceeded at an immoderate and excessive speed under the existing circumstances. They improperly failed to keep out of the way of *Sunima*. They improperly attempted to cross ahead of *Sunima*. They failed to ease, stop or reverse their engines in due time or at all. They failed to sound proper signals in accordance with the regulations. They failed to exercise the precautions required by the ordinary practice of seamen or by the special circumstances of the case. They failed to take in due time or at all proper or any steps to avoid the collision. They contravened Rule 18, 19, 22, 23, 25, 27, 28 and 29 of the *Regulations for Preventing Collisions at Sea.*

The case of the Defendants and Counter-Claimants is as follows:— The Defendants and Counter-Claimants, Villaneuve Compania Naviera, S.A. of Panama, are and were at the time of the collision hereinafter referred to, the Owners of the Liberian Steamship *Argyll* a steel, single screw cargo vessel registered at the Port of Monrovia, of 10657.46 tons gross and 6304 tons net register, 504' in length overall and 66.90' in breadth, equipped with steam turbine engines developing 7150 S.H.P. and manned by a crew of 37 all told. In the early hours of May 27, 1959, the *Argyll* whilst on a voyage from Port Alfred to Sorel in ballast, was proceeding up the River St. Lawrence, approaching the limits of the Harbour of Quebec where a change of pilots was going to take place. Her engines were turning at full speed with her telegraph on stand-by. The weather was fine and clear with good visibility and there was little or no wind. The tide was ebb and of a force of about 3 to 4 knots (Spring tide) flowing in an easterly direction. The *Argyll* was exhibiting the regulation navigating lights which were burning brightly, and a good lookout was being kept on board her. West Point Light at the western tip of Orleans Island was abeam at about 0200 on a course of 270° True and at 0203 the speed

was reduced to half. In these circumstances shortly after the reduction in speed, the masthead lights and green sidelight of a down-bound vessel which turned out to be the *Sunima* were sighted bearing about 25° on the port bow of the *Argyll* distant about 1¼ to 1½ miles. The *Argyll* kept on her course of 270° keeping well to her own side or north side of the channel, expecting to meet the *Sunima* red to red. Between 3 and 4 cables above Buoy 87½ B which was left 2 cables to port, the course of the *Argyll* was altered to 250° True in order to make the bend in the channel leading into the dock area of the Harbour of Quebec bringing Buoy 138B to bear fine on the starboard bow. The green light of the *Sunima* which then came to bear fine on the port bow of the *Argyll* was kept under close observation as those on board the *Argyll* expected the *Sunima* to manoeuvre so as to effect a port-to-port meeting. The *Sunima* however kept on showing her green shaping instead to be on a course crossing that of the *Argyll* from port to starboard at very close quarters, whereupon, as it became apparent that a collision would be unavoidable unless action was taken by the *Argyll*, the wheel of the *Argyll* was ordered hard-a-port and a signal of 2 short blasts blown. As the *Argyll* began to swing to port, the *Sunima* was observed to alter her course sharply to starboard closing her green and opening her red on the starboard bow of the *Argyll* and the collision occurred, the stem of the *Sunima* striking the starboard bow of the *Argyll* just abaft the stem. The engines of the *Argyll* were then stopped and by reason of the impact the swing of the *Argyll's* bow to port was accentuated and the *Sunima* continued to swing to starboard until both vessels came to head South, various manoeuvres being then made until both vessels were clear. The collision and the damage occasioned thereby to the *Argyll* were caused by the fault and negligence of the *Sunima* and those on board her as herein alleged: The navigators of the *Sunima* negligently and improperly failed to keep a proper and efficient lookout. They failed to keep to that side of the fairway which lay on their starboard side. They failed to alter course to starboard sufficiently or at all or in due time in order to effect a red to red meeting with the *Argyll*. They failed to keep out of the way of the *Argyll*. Generally, they failed to take the proper or any, or sufficient action with helm and/or engines in due time or at all. They failed to indicate signals and at the appropriate time the action which they actually took with helm and engines. The *Sunima* was proceeding at an excessive and immoderate rate of speed in contravention of the Regulations of the National Harbours Board in force in the Harbour of Quebec. The navigators of the *Sunima* failed to take in due time or at all proper or any steps to avoid the collision. They failed to exercise the precautions required by the ordinary practice of seamen and by the special circumstances of the case. The navigators of the *Sunima* contravened Articles 19, 22, 25, 28 and 29 of the *International Rules of the Road*, and Article 31 of the *National Harbours Board Regulations for the Harbour of Quebec*.

Evidence was brought on behalf of the Plaintiff that at 0152 the *Sunima's* engines were stopped, the vessel then being opposite the Pilot's station, and at 0155 Pilot Dionne came aboard. The engines were put full ahead at 0158, the ship then being about mid-channel almost opposite Queen's Wharf heading 023. The *Sunima* was kept on course 023 until abreast of Shed 26. Course was then altered to 030 and the vessel continued on 030 until Ste. Pétronille Light was open to the North with Buoy 89B. Her course was then altered to 050 on

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which course she continued until Shed 29 was slightly open with the inner Blue Light on the breakwater and as the *Sunima* passed the entrance to the St. Charles Basin the *Argyll* was first sighted, apparently in the vicinity of Ste. Pétronille Light and about two miles from the *Sunima*. The *Argyll's* mast lights and her red light were first sighted bearing about two points on the *Sunima's* starboard bow. At about that time the *Sunima* altered course to 070 and when the *Argyll's* leading lights came into line the *Sunima* altered another 10° to bring her onto course 080. At that time the *Argyll* was from ¾ of a mile to a mile distance and just abreast of Buoy 87½B. The *Sunima* then commenced to see the *Argyll's* green light and her red shutting out, whereupon the *Sunima* altered another 5° to starboard and seconds later sounded one short blast and put her helm hard astarboard just before the vessels collided. The *Argyll* appeared to go further to port, so the engines of the *Sunima* were ordered stopped and full astern. The stem of the *Sunima* hit the starboard bow of the *Argyll* 20 to 25 feet abaft the stem. The *Sunima*, at the time of the collision, was slightly South of mid-channel opposite a point midway between Lorne and Champlain dry-docks, a little East of and about 3 cables from the outfitting dock. The angle of collision was between 40 to 45 degrees and the time of collision about 0204 according to Pilot Dionne and Plaintiff's Preliminary Act.

Evidence adduced on behalf of Defendants and Counter-Claimants shows that the *Argyll* upward-bound went onto course 270 slightly below Marand Buoy and continued on this course past Ste. Pétronille Light (West Point) which she passed at a distance of about two cables. Her estimated speed over the ground at that time was twelve knots (full speed) there being an ebb tide giving a current of 3 to 4 knots. On the bridge with Pilot Goudreau were the Master and Wheelsman. The *Argyll*, when abeam of Ste. Pétronille Light at 0200, was put on stand-by and at 0203 her engines were put at half speed, she still being on course 270, and about two cables off and slightly below Buoy 87½B. Shortly thereafter the *Sunima* was first seen by those on board the *Argyll* at a distance of 1¼ to 1½ miles. The *Sunima's* green light and leading lights were first sighted about 3 points on the *Argyll's* port bow and those in charge of the *Argyll* estimated that the *Sunima* was on course 20° and 25°.

The *Argyll* continued on course 270 until she was about 5 cables above Buoy 87½B when she altered 20° to port to come onto course 250. After altering to course 250 those in charge of the *Argyll* saw the green light of the *Sunima* about 10° on the *Argyll's* port bow and her course was then estimated to be between 45° and 50° and her distance about 1¼ miles. According to Pilot Goudreau the alteration from course 270 to 250 occurred at 0205 hours. He testified that prior to this alteration he had Buoy 138B on his port bow and that after coming onto course 250 a buoy which was assumed to be Buoy 138B (but which may actually have been Buoy 140B) was about 10° on his port bow and he was still seeing the *Sunima's* green light. He then saw the leading lights of the *Sunima* closing so rapidly that he cried: "Oh, my God, to protect myself I will have to take action" so he went hard-a-port and about 7 or 8 seconds later the *Sunima* altered to starboard about one cable. The only time Pilot Goudreau saw the *Sunima's* red light was just prior to the collision. In giving his estimate as to the place where the accident occurred Pilot Goudreau expressed himself as follows: "We figured that we were about 5 cables above Buoy

87½ a mile and a cable above West Point which was bearing about 80 to 81°".

By Defendants Preliminary Act the place of collision is stated to have been "In the Harbour of Quebec well to the North of mid-channel line about 11 cables above West Point Light bearing 81°."

At the time of collision the *Argyll's* Pilot, Master and Wheelsman were on the bridge. Those in charge of the *Argyll* estimated that the collision occurred at about 0205 (although in Defendants' Preliminary Act the time is stated to have been between 0206 and 0207).

The evidence offered on behalf of Plaintiff as to the speed of the *Sunima,* courses steered by her and times of alteration of courses was not contradicted, and I am advised by the Assessors that they would have brought the *Sunima* to approximately that point at which, according to her Preliminary Act and the testimony of Pilot Dionne, the collision occurred.

There is no evidence to show that the *Sunima* was at any time to the North of mid-channel save and except for the calculations made by the *Argyll's* Pilot and Master as to the place of the collision.

The testimony of these witnesses however on this point is confused and, in particular, that of Pilot Goudreau appears to have completely disregarded and failed to take into account the *Argyll's* alteration from course 270 to 250 and the fact that the *Argyll* was undoubtedly on course 250 for upwards of two minutes prior to her going hard-a-port just prior to the collision.

There are, moreover, other reasons for believing that those in charge of the *Argyll* were in error in estimating the place of the collision.

Although these witnesses estimated that the *Argyll* passed West Point at a distance of 2 cables, I am convinced and, am so advised by the Assessors, that having regard to the testimony of Pilot Labrie, who was on the downbound Richard de Larrinaga which met the *Argyll* about ⅝ of a mile below West Point, the *Argyll* passed West Point at a distance of about 2.6 cables and that her speed from then until the collision occurred averaged not more than 10 knots over the ground, so that in the time of approximately 3 minutes it took the *Argyll* to cover the distance from a point opposite West Point to the place at which she altered course from 270 to 250 the *Argyll* had reached a point approximately abeam of and about 1.1 cables off Buoy 87½B instead of 5 cables above and 2 cables North of said Buoy, as estimated by Pilot Goudreau.

I find that the collision occurred at about 0205 hours.

It appears therefore that there elapsed approximately 3 minutes between the time at which the *Argyll* passed West Point until the time she altered course to 250 and about two minutes from the time the Argyll altered course to 250 until the collision occurred and that the *Argyll* in the course of approximately 5 minutes at an average speed which, I am convinced, would not have exceeded 8 to 10 knots an hour, would have covered not more than 8½ cables and that her position at the moment of the collision would have been South of mid-channel approximately 2.3 cables above Buoy 87½B, which position corresponds substantially with that testified to by those in charge of the *Sunima.*

On behalf of the *Argyll* it was urged that the *Sunima* was at fault, in that she was proceeding at an excessive speed in contravention of the legal limit which applies within the Harbour of Quebec. There is no doubt that the *Sunima's* speed was in excess of that permitted by law, but I am convinced that her speed was not the proximate cause or a

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contributing cause of the collision. On the contrary, I am satisfied that the casualty was brought about solely by the fault and negligence of those in charge of the *Argyll*, in that they improperly failed to keep to the side of the fairway or mid-channel which lay on their starboard side and instead of altering course to starboard, as they could and should have done when the *Sunima* was sighted, they altered to port in a manner which brought the *Argyll* on a course which crossed that of the *Sunima*.

Those on board the *Argyll* were, moreover, guilty of fault and negligence in failing to post a lookout on the bow of the vessel, having regard to the admitted difficulty of distinguishing ships' lights against the back-ground of the lights of Quebec City and harbour front. I have no doubt that the failure to post a lookout contributed to the bringing about of the collision, since I am convinced that the *Sunima* was not sighted by those in charge of the *Argyll* as soon as she should have been.

On the whole therefore I reach the conclusion that the collision was brought about solely by the fault, negligence and lack of seamanship of those in charge of the *Argyll*.

Plaintiff's action accordingly is maintained and Defendants' Counter-Claim is rejected, the whole with costs. Failing agreement by the parties as to the quantum of damages to which Plaintiff is entitled, there will be a reference to the Registrar for the purpose of having these damages fixed in accordance with the usual practice.

Judgment accordingly.

1961

Sept. 26

1962

May 18

BETWEEN:

THE STERLING TRUSTS CORPORATION and KATHLEEN DIGNAN, Executors of the Last Will and Testament and Codicils of ALAN DIGNAN

APPELLANTS;

AND

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

Revenue—Income—Income tax—Land purchased by private company as investment sold shortly thereafter at profit—Evidence of similar transactions—Funds distributed on winding-up deemed a dividend—Income Tax Act, R.S.C. c. 148, ss. 3, 4, 81(1) and 139(1)(e).

In 1951 D, a solicitor, acting on behalf of a private company which he later incorporated and of which he and his wife became sole owners, purchased a farm on the outskirts of Toronto for $52,000. The property was allegedly purchased as an investment and to serve as the site of the couple's future summer home but was disposed of in two separate sales in 1953 and 1954 at a substantial profit. Shortly thereafter the company was wound up, the proceeds from the sales distributed to the shareholders and the charter surrendered. The Minister treated the amount received by D as a profit from a business

and added it to the taxpayer's income. D's appeal from the assessment was dismissed by the Tax Appeal Board. Following D's death his executors brought a further appeal before this Court.

Held: That the evidence established that both prior to and after the sales now in question D had derived considerable profit from short-term purchases and sales of land in the same area. Private companies incorporated ostensibly to hold a single property for investment held it for a relatively short time and following sale the companies were promptly wound up and their assets distributed to their shareholders. This course of conduct helped to characterize the instant transaction as an undertaking in the nature of trade and served to indicate that D was engaged in a scheme of profit making.

2. That the proceeds in the company's hands following the sales in question constituted undistributed income which the Minister was justified in deeming a dividend within the meaning of s. 81 of the *Income Tax Act*.

APPEAL from a decision of the Tax Appeal Board.

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

R. B. Stapells for appellant.

W. G. Gray, Q.C. and *M. A. Mogan* for respondent.

KEARNEY J. now (May 18, 1962) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board[1] dated August 27, 1958 wherein the reassessment made by the Minister under the *Income Tax Act*, R.S.C. 1952, c. 148, in respect of the taxable income of the late Alan Dignan, Q.C. (hereinafter sometimes referred to as "the taxpayer"), of the city of Toronto, province of Ontario, for the year 1954 was affirmed and his appeal therefrom dismissed.

The taxpayer died on or about September 4, 1958. The Sterling Trusts Corporation and his widow, Kathleen Dignan, were appointed executors of his last will and testament and codicils and it is in their quality as such that they have instituted the present appeal.

The case arose because the taxpayer, acting on behalf of a company which he later caused to be incorporated as a personal corporation (hereinafter referred to as "the Company"), and in which he and his wife became owners of all of its issued capital stock, purchased, late in 1951, for the sum of $52,000, a parcel of land situated on the

[1] (1958) 20 Tax A.B.C. 247; 58 D.T.C. 555.

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outskirts of Metropolitan Toronto, Ontario, which the Company later disposed of in two separate sales, the last one having occurred early in 1954, thereby realizing $182,500.

Shortly thereafter, the Company was wound up and before surrendering its charter, for reasons which appear hereunder, it had on hand $119,609.11 for distribution to its shareholders, which amount the Minister regarded as a profit from a business and added it to the income of the taxpayer and which the appellants regard as a capital gain.

In addition to a submission that the proceeds from the two above mentioned sales constituted a capital appreciation and that no income resulted therefrom either to the Company or the taxpayer, the appellants, in paragraphs 7 and 8 of their notice of appeal, declared:

> 7. In the alternative, if the said Alan Dignan did receive a deemed dividend under the said Section 81(1) then the amount of such deemed dividend should be limited to his portion of the undistributed income on hand based upon his holdings of shares in the capital stock of the Company above set out.
>
> 8. In the alternative, if the said Alan Dignan did receive a deemed dividend under said Section 81(1), then the said assessment should be referred back to the Minister to be amended by him to allow the dividend credit pursuant to the provisions of Section 38 of the said Act.

The case was heard in September 1961, but later, at the request of counsel, permission was granted them to submit supplemental briefs, which were filed in February 1962. Apart from argumentation the said briefs disclosed that consideration of paragraphs 7 and 8 was not necessary because counsel agreed that the Minister, in arriving at the figure of $119,607.11, which he considered to be undistributed income under s. 81(1), had made due allowance for the respective shareholdings of the taxpayer and Mrs. Dignan and had granted the 20 per cent deduction as provided in s. 38(1) of the Act.

As a consequence, the amount of the alleged undistributed income of $119,609.11 is admitted by both parties, and the only issue is whether it constituted a capital appreciation, as claimed by the appellants, or a profit from a business of the Company within the meaning of ss. 3, 4 and 139(1)(*e*), which 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)(*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;

The relevant particulars are as follows.

As appears by an agreement of purchase and sale (Ex. 1) dated October 3, 1951, the late Alan Dignan, as trustee for a company to be formed, purchased a farm (hereinafter referred to as "the instant property"), which comprised 195 acres, located on lot 24 in the Township of North York, in the County of York, for the price of $52,000, on account of which he agreed to deposit with the vendor $1,000 on the signature of the deed and pay $2,000 on October 31, 1951 and $12,000 on the date of closing, and to cause the Company to give the vendor a mortgage of $37,000 on the property, with interest at 5 per cent payable $300 quarterly, and which would fall due five years from the date on which the sale was to be completed, viz., on or before November 30, 1951. The agreement also states:

It is agreed that the Vendor can remove the old frame barns on the north end of farm. The Vendor on paying of the taxes of the farm can occupy the house, barns and plant and remove crops until Oct. 1st 1952 the purchaser can sell any part of the land and camp on the property after the closing date of purchase.

The Offer includes all buildings and barns on lands herein, except old frame barns on north end of farm.

Mortgage given back on closing to be executed only by the Limited Company yet to be formed, but whose name will likely be ALANCO LTD.

All of the foregoing conditions were fulfilled but the intended name of the Company was unavailable, and on November 12, 1951, the taxpayer caused to be incorporated under the *Companies Act*, R.S.O. 1950, c. 59, a private company known as Norobshe Holdings Limited, the shares of which became beneficially held as follows:

THE TAXPAYER — 2,285 Preference Shares
par value: $10 each
3 Common Shares of N.P.V.

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KATHLEEN DIGNAN — 50 Preference Shares
3 Common Shares.

A secretary in the law office of the taxpayer held for him one of its Common Shares so that she could qualify as a third director in the Company to comply with the statutes of incorporation.

The charter of the Company (Ex. A) states that it was incorporated for the following purposes and objects—

(*a*) To acquire and hold as an investment the instant property.

(*b*) To charge on mortgage the said lands.

(*c*) To invest in certain types of shares and bonds.

On July 19, 1953, the Company sold to James Metcalfe, a lawyer friend of the taxpayer, 100 acres of the said property for $40,000 and the remaining 95 acres were disposed of on January 10, 1954 to Central Mortgage and Housing Corporation for the sum of $142,500. Shortly thereafter, a distribution of the sum of $119,609.11 was made to the shareholders, as previously stated, and the Company surrendered its charter in March 1954.

The late Alan Dignan was the chief witness for the appellants and certain indicated pages of the transcript of the testimony given by him before the Income Tax Appeal Board were filed, by consent of the parties, as evidence in this Court.

On examination in chief he stated that he and his wife were desirous of acquiring a piece of property not too far from where they lived for the personal use and benefit of themselves and family. He saw an advertisement in a newspaper offering for sale a property situated west of Yonge Street, and, after inspecting it, decided to buy it as an investment, with the intention of using it for picnicking during the summer and ultimately building a summer home upon it. The reason, he said, why so large a property was acquired was because the owner would not sell less than the totality of its 195 acres. The witness further stated that, seeing he and his wife did not have sufficient ready money to pay the purchase price in cash, he intended to rent the farm with outbuildings as means of meeting the interest due on mortgage.

His reason, he said, for causing the holding company to be incorporated and having it acquire the instant property was to enable him and his wife to escape personal responsibility for the $37,000 mortgage mentioned in Exhibit 1.

According to the taxpayer, the Company did not seek to sell the land or make any offer to do so and the sale in July 1953 of 100 acres thereof to a lawyer friend was unsolicited and was accepted because the acreage in question was the least attractive part of the property and because the proceeds of the sale, amounting to $40,000, served to substantially reduce the outstanding mortgage.

In respect of the sale of the remainder of the property, on the 10th of January 1954, to Central Mortgage & Housing Corporation for $142,500, the taxpayer testified that the Company was approached by an agent of Central Mortgage & Housing Corporation who was attempting to acquire for the latter a block of some 600 acres for the purpose of building a low-cost-housing scheme and it so happened that the instant property was located in the very centre of the proposed parcel. Since a low-cost-housing centre would spoil the property as a housing site for its shareholders and because the property could be made subject to expropriation proceedings, the Company decided to accept the offer.

In the opinion of the taxpayer, the immediate vicinity where the Company property was located was, neither when purchased nor in 1958 when the witness's evidence was given, suitable for building development. Having disposed of the property for which the Company had been incorporated, its shareholders decided to wind it up and distribute its assets. Whereupon the Dignan family purchased another country retreat of some 90 acres, further north, at Bolton, to replace what the taxpayer described as "the lost property" and which they still had in their possession at the time their testimony was given.

As appears on cross-examination, the instant property is located immediately to the west of the Township of Etobicoke, which is another suburban area within the Municipality of Toronto. The taxpayer had practised his profession in Toronto mainly as a corporation lawyer for thirty-four years; for six years, beginning in 1947, he was a member of the Planning Board of the Township of Etobi-

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coke and chairman of it during three of those years; he had occasion to conduct a study of land use in Etobicoke and had set up the official plan for zoning and land-use-control therein.

The taxpayer also stated that he hoped to pay for carrying charges by renting the property but that he was disappointed in this hope. In point of fact, taxes alone amounted to $700 per annum, the other carrying charges to about $1,800, and the revenue, consisting of rentals, was less than $500 per annum. The witness admitted that he had made no enquiry as to the possible rental value of the property prior to its purchase.

The witness acknowledged that he had done title work for Central Mortgage & Housing Corporation, but declared that this had only occurred after the Company had sold the remaining 95 acres of the instant property to Central Mortgage & Housing Corporation, as already indicated. He could not explain why Exhibit 1 contained the provision permitting the purchaser *to sell* "any part of land . . . after the closing date of purchase", as referred to in para. 5 *supra*. He admitted that in the spring of 1953 he had instructed a real estate agent to find a buyer for the 100 acres which were sold in July 1953.

Mrs. Dignan also testified, and her evidence, apart from corroborating her late husband's testimony mainly in the following details, added little to what he had said. She stated that the family, since 1949, had been looking for a country property and during the summers of 1952 and 1953 made use of it for picnics practically every week-end; that the Company was forced to sell it because of the Government (presumably this refers to possible expropriation proceedings by Central Mortgage & Housing Corporation); that immediately following the sale the family bought a property in Bolton for some $5,000 to replace it and where a modest home was built, and which she and her three children still hold and use. She was vice-president of the Company and the 50-Preferred and 3-Common shares which she acquired she paid for with her own money. The only property in which she had an interest as a joint-tenant or as a shareholder was the property in question; that the other properties hereinafter mentioned in which

her late husband had an interest were either owned by him alone or with others and that she never had an interest in any of her late husband's business affairs.

The third and last witness called by the respondent was R. G. Parker, officer of The Sterling Trusts Corporation, who stated that the subject property which had been acquired by Central Mortgage & Housing Corporation was still undeveloped rural property at the time his testimony was given. I might here observe that no evidence was adduced one way or the other to explain why the Central Mortgage & Housing Corporation, after having made the large purchase of 600 acres already mentioned, had not, up to the time of trial, proceeded with their proposed low-cost-housing development. It may be that they purchased it to curtail too rapid suburban development and speculation therein.

The only witness called by the respondent was Eric J. Hunter, auditor, who was in charge of the investigation of the taxpayer's income tax return and had been employed for seventeen years with the Income Tax Division, Department of National Revenue. Exhibit 2 contains a list of purchases and sales of real estate, dating from 1949 to 1958, in which the taxpayer was an interested party. The following are some of the more noteworthy of such transactions and which occurred in the years immediately prior and subsequent to the purchase and sale of the instant property and concerning which Mr. Hunter commented.

(*a*) On July 3, 1950, the taxpayer, P. J. Anderson and W. T. Vance purchased lot 20, concession 2, in the Township of Etobicoke, which consisted of vacant land, for $87,680, on the following terms: $25,000 cash and a mortgage given back for $62,680.

On March 31, 1952, they sold the said land at a net profit of $7,737.47 to each of the said owners.

(*b*) On June 4, 1952, Alan Dignan, as trustee for the under mentioned group, purchased from George Thurkle lot 16, concession 3, Township of Etobicoke, consisting of vacant land, for $55,000 cash. The owners of the said property were—

W. T. Vance —to the extent of $\frac{1}{3}$ interest

P. J. Anderson
Alan Dignan
P. J. Walsh
J. Weil
} —to the extent of $\frac{1}{6}$ interest each

The property was sold on April 22, 1953 for $100,000, of which $30,000 was paid in cash and a mortgage given for the remainder, and the taxpayer realized a net gain thereon of $7,359.39.

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(c) In 1954 the taxpayer entered into an agreement with one Davis to purchase part of lot 12, First Meridian Concession, Township of Etobicoke, for the sum of $174,225, the terms being—cash, $92,960, and a mortgage back to the vendor for $81,265.

Subsequently, on June 2, 1954, he caused to be incorporated Vanal Holdings Limited, a company which, according to its charter, was incorporated for the purpose of acquiring and holding as an investment the above mentioned property which he caused to be transferred to it; whereupon the taxpayer became the owner of 70 per cent of the shares of the Company, the remaining 30 per cent was issued to W. T. Vance.

On April 21, 1955, the Company sold a portion of the said property to Finley W. McLachlan Limited for $100,422. The terms were—cash, $47,422, and a mortgage given back for $53,000.

On the same date, 3.2 acres were sold to the Township of Etobicoke for $11,577.63.

On April 22, 1955, the balance of the property, amounting to 12,100 acres, were sold to Dominion Paper Box Limited for $103,000 cash. The taxpayer's share of the net profits amounted to $19,827.56.

Subsequently in 1955, Vanal Holdings Limited was wound up and surrendered its charter.

It also appears, *inter alia,* by the evidence that the taxpayer purchased two properties in trust, for $82,000 and $60,000 respectively, and on November 1, 1953 he conveyed the first one to Burnhamthorpe Holdings Limited and the second to Alanthorpe Holdings Limited. Alan Dignan held one Common Share out of six in the capital stock of each of the companies. He disposed of them on March 19, 1956. The said properties have been retained by the said companies and the profit or loss, if any, which the taxpayer derived is unknown.

In support of his submission that appellants have discharged the onus which rested on them to show that the Company did not realize a taxable profit on the sale of its sole asset, counsel for the appellants contended that the evidence adduced clearly proves that the only purpose which the taxpayer and his wife had in acquiring the property in question was to hold it, for their own use and enjoyment, as a week-end picnic site, until they were able to build a house on it, which they expected to do in five or seven years; that the Company at no time did any development work nor did it intend to do so; neither did it, except in respect of the Metcalfe transaction, list the property for sale with any real estate agent; that this latter transaction, which was made more than a year and a half after the property had been acquired, was accidental and

unforeseen; and that the sale of the remainder of the property, about six months later, was unlooked for and forced upon the Company by, likely, expropriation proceedings on the part of Central Mortgage & Housing Corporation.

The appellants' case is almost entirely dependent on the evidence given by the taxpayer. The following observations made by Thorson P. in *Minister of National Revenue v. L. W. Spencer*[1], I think, are applicable in the present case:

> ...It is well established that a taxpayer's statement of what his intention was in entering upon a transaction, made subsequently to its date, should be carefully scrutinized. What his intention really was may be more nearly accurately deduced from his course of conduct and what he actually did than from his *ex post facto* declaration.

It is to be noted that, in the course of his testimony, the taxpayer stated that he did not have the intention of selling the property "the minute it was bought" and that it never occurred to him that he did not really require the whole of the 200 acres. I think the fact that the original agreement of purchase (Ex. 1) provides that the purchaser "can sell any part of the land" after the closing date of the purchase is an indication that the taxpayer's mind was, by no means, oblivious to the possibility or likelihood of resale, particularly as he was at a total loss to explain why the provision was inserted. He stated that when he purchased the property he did not know nor was he concerned with the price which was being asked for it, but handed to Mr. Waddington, the agent for the vendor, his own offer of purchase which was later accepted and at which price he thought it was a good buy. This, I think, shows that the taxpayer was thoroughly familiar with land values in North York and had every confidence in his own valuation. This was only to be expected in view of the position he held on the Municipal Planning Board of nearby Etobicoke County and the success which he had experienced in previous real estate transactions in that township. In the circumstances I think it is most improbable that at the time of the purchase the only object which the taxpayer had in mind in buying the property was to keep it as a rest retreat for five or seven years and then utilize it as a site for a summer home and that he did not, as was said by Thurlow J. in

[1] [1961] C.T.C. 109 at 132.

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Bayridge Estates Ltd. v. Minister of National Revenue[1], have "in mind the most obvious alternative course open for turning the property to account for profit."

In their notice of appeal the appellants allege that among the reasons why the Company accepted the Metcalfe offer was because the whole 200 acres was not necessary for the purpose of building a country home and the portion sold to Mr. Metcalfe was less desirable than the remainder of the property. This is somewhat at variance with the taxpayer's reply, on cross-examination, to the following question:

> Q. When you found that you had to buy the whole piece in order to get any of it, did it occur to you at the time that although you had to buy the whole piece that you might not really need to retain the whole piece for your purposes?
>
> A. No, sir.

The taxpayer, in his testimony, declared that the property was purchased as an investment; it was certainly not an investment in the sense that it yielded a net revenue, and if, before the purchase, he had been sufficiently concerned to make enquiries, he would have ascertained that the carrying charges were five times greater than the revenue.

Because they are so numerous, it is needless for me to cite authorities to justify saying that each case must be judged on its own merits and the important question is the proper deduction to be drawn from the whole course of conduct of the taxpayer in the light of all the circumstances. As far as I am aware, it has never been challenged that evidence of prior transactions similar to the one in issue is admissible to prove a course of conduct tantamount to carrying on a trade or an adventure in the nature of trade. I think the same is true in respect of similar subsequent transactions. In *Rosenblatt v. Minister of National Revenue*[2], Ritchie J., p. 12, observed:

> I entertain no doubt as to the admissibility of evidence respecting subsequent transactions in order to establish that the particular transaction under consideration marked the commencement of a series of similar transactions or of a course of conduct in the nature of a trade or business.

[1] [1959] Ex. C.R. 248 at 255. [2] [1956] Ex. C.R. 4.

I have already had occasion to concur in the above-mentioned finding; *vide, Archibald v. Minister of National Revenue*[1]. Ritchie J. in *Minister of National Revenue v. Pawluk*[2] also stated:

> It is my view that on income tax appeals evidence may be received in respect to any matters that have occurred *up to the time of the actual hearing* of the appeal, provided such matters have relevancy to the taxation year to which the assessment, or reassessment, under appeal applies. (The italics are mine.)

In the instant case the taxpayer had derived considerable profit, more particularly from two prior and one subsequent transactions involving short-term purchases and sales of vacant land in the same area. Both Norobshe Holdings Limited and Vanal Holdings Limited, although each incorporated ostensibly to hold a single property for investment, held it for a relatively short time, and following its sale the companies were promptly wound up and their assets distributed to their shareholders. I might here interpose that, in my opinion, the restricted nature of the purposes and objects of these companies, as set out in their Letters Patent, has very little weight insofar as the establishment of the taxpayer's intent is concerned. Norobshe Holdings Limited, apart from the powers set out in its Letters Patent, possessed broad incidental and ancillary powers by virtue of R.S.O. 1950, c. 59, s. 23, including the right to acquire and carry on any other business calculated to enhance the value of or render profitable any of the Company's property or rights; and to purchase or otherwise acquire any property or business which it may think necessary or convenient and to sell and dispose of the whole or any part thereof. In his testimony the taxpayer stated that he was aware of and relied upon such ancillary powers.

As already noted, the taxpayer declared that his sole purpose in making use of a corporate set up was so that he and his wife might avoid personal responsibility for the repayment of a mortgage. As noted previously, it also served, in the event that the $119,609.11 were held to be taxable income upon its distribution, to reduce by 20 per cent the tax which would have been payable had the instant property been registered in the name of the taxpayer and his wife. Likewise, the manner in which the subscription to the share capital of the Company was made

[1] [1961] Ex. C.R. 275 at 280. [2] [1956] Ex. C.R. 119 at 123.

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Kearney J.

enabled the taxpayer's wife, following the redemption of all the preferred stock and when the Company surplus assets were distributed, to receive a sum equal to that of her late husband, namely, almost $60,000, at relatively little cost to her. Furthermore, the winding up of the Company was facilitated because the taxpayer restricted its assets to the ownership of the instant property.

I think it is clear that the taxpayer was interested and showed ingenuity in minimizing the incidence of income tax. Of course, as Kerwin, C.J., observed in *Curran v. The Minister of National Revenue*[1] (p. 854):

> Under the authorities it is undoubted that clear words are necessary in order to tax the subject and that the taxpayer is entitled to arrange his affairs so as to minimize the tax. However, he does not succeed in the attempt if the transaction falls within the fair meaning of the words of the taxing enactment.

Although successful to the extent above indicated, I do not think that the taxpayer can escape the consequences of the instant assessment.

One frequently hears in ordinary parlance the expression: "It is all right if you don't make a business of it."

The evidence shows that during a period of five years the taxpayer engaged in interlocking purchases and sales of vacant land of a speculative nature, which occurred near the extremities of Metropolitan Toronto—so we are not here dealing with an isolated instance such as fell for decision in *Irrigation Industries Limited v. The Minister of National Revenue* (unreported judgment rendered on March 26, 1962) and in which the taxpayer was successful.

The *modus operandi* of the taxpayer, through the medium of partnerships or companies which he caused to be incorporated, helped to characterize the transactions as "undertakings in the nature of trade" and served to indicate that he was engaged in a scheme of profit making.

I think, as was said by Judson J. in *Regal Heights Limited v. The Minister of National Revenue*[2], affirming the judgment of Dumoulin J., "it was not an ordinary investment but an operation of business in carrying out a scheme of profit-making."

[1] [1959] S.C.R. 850. [2] [1960] S.C.R. 902; [1960] Ex. C.R. 194.

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It is true that in the instant case the taxpayer was unable or refrained from doing any development work on the property; but, since it was being carried at an annual loss, this strongly suggests an unexpressed intention to sell it, and I think the following statement made by the trial judge in the *Regal Heights* case (*supra*) is apposite:

> Throughout the existence of the appellant company, its interests and intentions were identical with those of the promoters of this scheme.

For the foregoing reasons I consider that the sum of $119,609.11 constituted undistributed income in the hands of the Company; that the Minister was justified in deeming it to be a dividend within the meaning of s. 81; and that the reassessment made against the taxpayer was justified. The appeal will be dismissed with costs.

Judgment accordingly.

1960

May 31

1962

Apr. 26

May 28

BETWEEN:

WEST YORK COACH LINES LIMITED ..... APPELLANT;

AND

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

Revenue—Income—Income Tax Act, R.S.C. 1952, c. 148, s. 20(1) & (6)(g)—Bulk sale of assets—Proceeds of sale of depreciable property held taxable in virtue of s. 20(6)(g) of the Income Tax Act—Appeal dismissed.

Appellant disposed of its business assets and good-will to the Toronto Transit Commission for the sum of $450,000 without allocating any portion of the total purchase price to the fixed assets, buses, equipment and goodwill respectively. It contended that only $65,187.53 could be considered as paid for the buses, the depreciable assets of the business.

The respondent assessed the appellant for $172,300 of the purchase price relying on the evidence of two expert valuers who had advised the Toronto Transit Commission that in their opinion the buses were worth $172,300. An appeal to the Tax Appeal Board was dismissed and appellant now appeals to this Court.

Held: That $172,300 is that part of the total consideration of $450,000 that can reasonably be regarded as being the consideration for the disposition of the buses and this amount is deemed to be the proceeds of the disposition of the appellant's depreciable property within the meaning

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of s. 20(1) of the Act "irrespective of the form or legal effect of the contract or agreement" between appellant and the Toronto Transit Commission.

2. That the respondent was right in assessing appellant as he did and the appeal must be dismissed.

APPEAL under the *Income Tax Act.*

The appeal was heard before the Honourable Mr. Justice Cattanach at Ottawa.

Stuart Thom, Q.C. for appellant.

E. A. Goodman, Q.C. and *D. Andison* for respondent.

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

CATTANACH J. now (May 28, 1962) delivered the following judgment:

This is an appeal from the decision of the Income Tax Appeal Board[1] dated June 19, 1959, dismissing the appellant's appeal from its income tax assessment for its taxation year ending January 31, 1955.

The appellant, West York Coach Lines Limited, operated bus services in the suburban areas of the City of Toronto, as well as a charter bus business. The real property used in connection with the bus operations was owned by an affiliated company, West York Motors Limited. In 1953 the Ontario Municipal Board concurred in an application for the amalgamation of the City of Toronto with surrounding municipalities and the recommendations of the said Board were enacted into law by c. 73 of the *Statutes of Ontario,* 1953. The sections of the said statute relating to public transportation include the following:

102. On and after the 1st day of January, 1954, there shall be a commission to be known as Toronto Transit Commission, with the powers, rights, authorities and privileges vested in it by this Act.

109. (2) Except in accordance with an agreement made under subsection 3, no person other than the Commission shall, after the 1st day of July, 1954, operate a local public passenger transportation service within the Metropolitan Area, with the exception of steam railways and taxis.

(3) An agreement may be entered into between the Commission and any person legally operating a local public passenger transportation service wholly within or partly within and partly without the Metropolitan Area on the 1st day of January, 1954, under which such person may continue to operate such service or any part thereof for such time and upon such terms and conditions as such agreement provides.

[1] (1959) 22 Tax A.B.C. 171.

(5) Where a local public passenger transportation service is legally operating partly within and partly without the Metropolitan Area on the 1st day of April, 1953, and continues in operation, and will be required by subsection 2 to cease to operate within the Metropolitan Area on the 1st day of July, 1954, or upon the termination of an agreement made under subsection 3,

(a) the Commission may agree with the owner of the service, not later than one month before the date upon which the service will be required to cease to operate within the Metropolitan Area, to purchase the assets and undertaking used in providing the entire service or to purchase the portion thereof that is allocated to the provision of the service within the Metropolitan Area;

Negotiations were begun by the Toronto Transit Commission for the acquisition of the business and undertaking carried on by the appellant, plus the real estate owned by West York Motors Limited, used in conjunction with its bus operation. An offer of $250,000 was made by the Toronto Transit Commission during the first part of June, 1954, which was refused by the appellant. A subsequent offer of $450,000 was made on or about June 15, 1954, which was acceptable to the appellant (this amount being suggested by the appellant as the proper amount) and culminated in an agreement of sale dated June 21, 1954, between the appellant and West York Motors Limited as vendors and the Toronto Transit Commission. The agreement provided for the payment of $450,000 for all the assets, together with all goodwill in respect of the bus services, including charter services, the take-over date being July 1, 1954. It was not recorded how much of the total purchase price was to be allocated to the fixed assets, buses, equipment and goodwill respectively.

Prior to entering into the agreement dated June 21, 1954, the Toronto Transit Commission employed two persons to evaluate the buses owned by the appellant. The first was E. M. Hurst, president of Bus Sales of Canada, Limited, and eastern representative of Motor Coach Industries, Limited, manufacturers of highway buses; and the second was G. S. Gray, who was Transit Controller for Canada during the war years and subsequently vice-president in charge of sales for a bus manufacturing company. On March 23, 1954, these two appraisers placed a valuation of $172,300 on the appellant's buses.

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In compiling its income tax return for the fiscal period ending January 31, 1955, the appellant reported the sum of $65,187.53 as the proceeds of the disposition of the buses, being the amount at which the buses were carried in its books.

When re-assessing the appellant, the notice of re-assessment being dated January 28, 1957, the Minister took the sum of $172,300 as representing the amount paid to the appellant for the buses, instead of $65,187.53, and applied the recapture of capital cost allowance provisions of the *Income Tax Act* accordingly.

The appellant filed a notice of objection to the aforesaid re-assessment and by notice dated November 29, 1957, the Minister confirmed the assessment on the ground that

> under the provisions of paragraph (*g*) to subsection (6) of section 20 of the Act it has been determined that $172,300 of the amount received by the taxpayer from Toronto Transit Commission pursuant to an agreement dated 21st June, 1954 was for buses and therefore the amount added to the taxpayer's income under subsection (1) of section 20 of the Act has been correctly determined.

The appellant appealed to the Income Tax Appeal Board which dismissed its appeal. It is from that decision that the appeal to this Court is brought.

The relevant provisions of the *Income Tax Act*, R.S.C. 1952, c. 148, are as follows:

> 20. (1) Where depreciable property of a taxpayer of a prescribed class has, in a taxation year, been disposed of and the proceeds of disposition exceed the undepreciated capital cost to him of depreciable property of that class immediately before the disposition, the lesser of
>
> (*a*) the amount of the excess, or
>
> (*b*) the amount that the excess would be if the property had been disposed of for the capital cost thereof to the taxpayer,
>
> shall be included in computing his income for the year.
>
> 20. (6) For the purpose of this section and regulations made under paragraph (*a*) of subsection (1) of section 11, the following rules apply:
>
> (*g*) Where an amount can reasonably be regarded as being in part the consideration for disposition of depreciable property of a taxpayer of a prescribed class and as being in part consideration for something else, the part of the amount that can reasonably be regarded as being the consideration for such disposition shall be deemed to be the proceeds of disposition of depreciable property of that class irrespective of the form or legal effect of the contract or agreement; and the person to whom the depreciable property was disposed of shall be deemed to have acquired the property at a capital cost to him equal to the same part of that amount; . . .

The issue in the appeal is whether the amount of $172,300 is that part of the total amount of $450,000, which the appellant received from the Toronto Transit Commission, that can reasonably be regarded as being the consideration for the disposition of the appellant's buses which were its depreciable property. If it can be so regarded, the amount shall be deemed to be the proceeds of the disposition of its depreciable property, within the meaning of s. 20(1) of the Act.

In my opinion, the amount of $172,300 can reasonably be regarded as being the consideration for the disposition of the buses, within the meaning of s. 20(6)(*g*) of the Act.

There are ample grounds for this conclusion. The Toronto Transit Commission employed two independent and qualified appraisers to make an evaluation of the buses before they made their offer of $450,000 for the appellant's whole enterprise. Their valuation of $172,300 was the amount at which the buses were taken into the books of the Toronto Transit Commission at the time of the purchase.

According to Mr. J. H. Kearns, the treasurer of the Commission, this amount was so entered because it was the amount of the appraisal, and Mr. Kearns also stated that out of the purchase price of $450,000, $172,300 was allocated to the buses.

In view of the conclusion that $172,300 is that part of the total amount of $450,000 that can reasonably be regarded as being the consideration for the disposition of the buses, it follows that this amount is deemed to be the proceeds of the disposition of the appellant's depreciable property, within the meaning of s. 20(1) of the Act "irrespective of the form or legal effect of the contract or agreement between the appellant and the Toronto Transit Commission". The Minister was, therefore, right in reassessing the appellant as he did, and its appeal herein must be dismissed with costs.

Judgment accordingly.

1960
Nov. 16
1962
April 2
June 8

BETWEEN:

EDWIN L. SCHUJAHN ..... APPELLANT;

AND

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

Revenue—Income Tax Act, R.S.C. 1952, c. 148, ss. 29, 139(4)—Appellant not "ordinarily resident" in Canada from date of his removal to United States of America though his family remained in Canada to end of that year—Appeal allowed.

Appellant, a United States citizen employed by a corporation of that country was moved to Toronto, Ontario by his employer in 1954. He purchased a house in Toronto and lived there with his wife and family until he was promoted to a higher position in the company in July 1957. He left Toronto for Minneapolis on August 2, 1957 taking only his personal effects with him. As he was unable to sell his house at that time he left his wife and children in Toronto in order that the house would not be vacant and so easier to sell. He resigned his club membership in Toronto. The house was sold in February, 1958, at which time his family rejoined him in the United States. Between August 2, 1957 and the end of the year 1957, the appellant was in Canada only three times, for a week-end on his way overseas, for a few days on his return and for a week at Christmas. The respondent assessed appellant for tax on his full 1957 income, from which assessment he appealed to this Court.

Held: That the appellant ceased to be resident or "ordinarily resident" in Canada in August 1957 despite the fact that his wife and son remained in Canada until the sale of his house, and therefore is entitled to the deductions allowed by s. 29 of the *Income Tax Act*, R.S.C. 1952, c. 148 from August 2, 1957 to the end of the year.

APPEAL under the *Income Tax Act.*

The appeal was heard before the Honourable Mr. Justice Noël at Ottawa.

D. A. Hanson for appellant.

Paul Boivin, Q.C. and *Roger Tassé* for respondent.

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

NOËL J. now (June 8, 1962) delivered the following judgment:

This is an appeal under the *Income Tax Act* R.S.C., 1952, c. 148, from an assessment for the year 1957 and turns on the question as to whether the appellant was residing or ordinarily resident in Canada during the whole of such year.

The appellant is an American citizen who worked and lived in Minneapolis, in the United States of America, until the year 1954. He is employed by General Mills Inc., a company with world-wide affiliations and whose head office is situated in Minneapolis, U.S.A. The company decided to start doing business in Canada in the year 1954 and purchased a piece of land in Toronto on which it built a plant; in the year 1954 the appellant was transferred from Minneapolis, U.S.A., the American parent company, to the Canadian subsidiary in Toronto, for the purpose of taking charge of the Canadian operations. Upon leaving with his family he gave up his resident membership in a Minneapolis club and moved to Toronto where he purchased a house at 38 Lambeth Road. He and his family lived in Toronto at the above address from the year 1954 to August 2, 1957 upon which date he was recalled and returned to the parent company in Minneapolis as assistant to the Vice-President. His wife and one son, however, remained in Toronto in their home until it was sold in February 1958 because, as he explained, "he had been advised that it would be difficult to sell an empty house, more difficult than one that was lived in, and the market was badly depressed." On this sale he sustained a loss of $6,000. The appellant upon hearing of his transfer back to Minneapolis contacted, in July 1957, a firm of real estate agents in Toronto, Kay & Fenn, and told them to try to sell his house. He also resigned his family membership in the Granite Club in Toronto. Upon his arrival in Minneapolis, U.S.A., he sought residence there and took with him his clothes, radio and his photographic equipment, which appears to be a hobby with him. He took steps to rejoin a club he formerly belonged to in Minneapolis as a resident member. He also states that he had been advised by senior officers of General Mills Inc. that his recall to Minneapolis was on a permanent basis.

He had a car of his own which he took with him to Minneapolis but until February 1958, he left a car in Toronto which his wife used but which was registered in his name. He admits also of having a small bank account with the Royal Bank in Toronto during the period of August 2, 1957 to December 31 of the same year for the purpose of paying mortgage payments on his home and other bills, and a smaller account with the Bank of Nova Scotia which

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his wife used for household bills. This last account would probably run up to as high as $200 at a maximum at any time.

Between August 2, 1957 and the end of 1957 he was in Toronto on three occasions only: (1) early in October or late September 1957 on his way to a business trip to England (for a weekend); (2) on his way back to the States, he flew Trans-Canada direct to Toronto (spent 3 or 4 days); (3) he came back for the Christmas holidays (spent a week). In the meantime, he lived until Christmas of 1957 in the Minneapolis Athletic Club in Minneapolis, U.S.A., but after Christmas moved into a small hotel, the Sheraton.

An agreement to sell his house in Toronto was signed on January 10, 1958, the settlement accomplished on February 25, 1958 and the next day, February 26 of the same year, his wife and son joined him in Minneapolis, U.S.A. Upon his wife's and son's arrival in Minneapolis in February 1958, they bought a house and signed the papers in the month of March 1958, and as he puts it "as soon as she came down, she took over the job of finding a house and we own a house there now".

The only matter in dispute between The Minister of National Revenue and the appellant is as to whether or not the latter was a resident of Canada for the whole of the year 1957 or, to put it more concisely, whether he remained a resident of Canada from and after August 2, 1957. The appellant admits that for the taxation year 1957, which is in appeal, up until August 2, 1957, he was a resident in Canada for income tax purposes within the meaning of section 139(4) of the *Income Tax Act*. However, he submits that when he left Toronto on August 2, 1957, to take another appointment in the United States, he then ceased as of that date to be a resident of Canada and that, consequently, he is entitled to the benefits of section 29 of the *Income Tax Act* and should not report as income the revenue he has earned in the United States from August 2, 1957 to December 31, 1957. Sections 139(4) and 29 of the *Income Tax Act* read as follows:

139(4) In this Act, a reference to a person resident in Canada includes a person who was at the relevant time ordinarily resident in Canada.

29. Where an individual was resident in Canada during part of the taxation year, and during some other part of the year was not resident in Canada, was not employed in Canada and was not carrying on business in Canada, for the purpose of this Act, his taxable income for the taxation year is

(*a*) his income for the period or periods in the year during which he was resident in Canada, was employed in Canada or was carrying on business in Canada computed as though such period or periods were the whole taxation year

minus

(*b*) the aggregate of such of the deductions from income permitted for determining taxable income as may reasonably be considered wholly applicable to such period or periods and of such part of any other of the said deductions as may reasonably be considered applicable to such period or periods.

The terms "resident" and "ordinarily resident" have been the subject of a number of decisions in the English courts, in the Exchequer Court and the Supreme Court of Canada. A very able and thorough study of these decisions has been made in a judgment of the learned President of the Exchequer Court, in the case of *Percy Walker Thomson and The Minister of National Revenue*[1], which was confirmed by the Supreme Court of Canada[2]. In both these decisions, a number of cases dealt with by the English courts and some Canadian decisions were analyzed and it is possible to draw from them a number of conclusions of which some may be applicable to the present instance. There is no definition in the act of "resident" or "ordinarily resident" and these terms should receive the meaning ascribed to them by common usage.

It is quite a well settled principle in dealing with the question of residence that it is a question of fact and consequently that the facts in each case must be examined closely to see whether they are covered by the very diverse and varying elements of the terms and words "ordinarily resident" or "resident". It is not as in the law of domicile, the place of a person's origin or the place to which he intends to return. The change of domicile depends upon the will of the individual. A change of residence depends on facts external to his will or desires. The length of stay or the time present within the jurisdiction, although an element, is not always conclusive. Personal presence at sometime during the year, either by the husband or by the wife and family, may be essential to establish residence within it. A residence

[1] [1945] C.T.C. 63. [2] [1946] S.C.R. 209.

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Noël J.

elsewhere may be of no importance as a man may have several residences from a taxation point of view and the mode of life, the length of stay and the reason for being in the jurisdiction might counteract his residence outside the jurisdiction. Even permanency of abode is not essential since a person may be a resident though travelling continuously and in such a case the status may be acquired by a consideration of the connection by reason of birth, marriage or previous long association with one place. Even enforced coerced residence might create residential status.

From this it follows that the terms "resident" and "ordinarily resident" are very hard to define and as put by Rand J. in re *Thomson and The Minister of National Revenue*[1]:

> The gradation of degrees of time, object intention, continuity and other relevant circumstances, shows, I think, that in common parlance "residing" is not a term of invariable elements, all of which must be satisfied in each instance. It is quite impossible to give it a precise and inclusive definition. It is highly flexible, and its many shades of meaning vary not only in the contexts of different matters, but also in different aspects of the same matter. In one case it is satisfied by certain elements, in another by others, some common, some new. The expression "ordinarily resident" carries a restricted signification, and although the first impression seems to be that of preponderence in time, the decisions on the English Act reject that view. It is held to mean residence in the course of the customary mode of life of the person concerned, and it is contrasted with special or occasional or casual residence. The general mode of life is therefore relevant to the question of its application.

And at p. 225 he adds:

> Ordinary residence can best be appreciated by considering its antithesis, occasional or casual or deviatory residence. The latter would seem clearly to be not only temporary in time and exceptional in circumstances but also accompanied by a sense of transitoriness and of return.

It was decided in *Murphy In re Income Tax Act (Manitoba)*[2] that:

> To determine whether a person has ceased to be resident of any particular place, the duration of his previous residence, his connections with that community and his interest in it are circumstances to be considered.

The English decisions however from which many of the above-mentioned findings have been drawn are subject to some reserve in that the finding of the Commissioners on a question of fact is final and cannot be reviewed by the

[1] [1946] S.C.R. 224.

[2] (1933) 41 Man. Rep. 621.

higher courts, the jurisdiction of which is limited to questions of law only. And in many of these English cases Their Lordships stated that they felt that although they would have probably come to a different conclusion had they been the Commissioners they could not possibly intervene.

The situation before this Court is of course different. The Court can hold, based on the facts disclosed by the evidence, that the appellant was or was not resident or ordinarily resident in Canada during the period under review. It was also pointed out in the *Thomson* case that Rule 3 of the General Rules applicable to all the Schedules of the English *Income Tax Act* may have had an effect on the result arrived at in some of the English cases.

Indeed this rule provides:

> That every British subject whose ordinary residence has been in the United Kingdom shall be assessed and charged to tax notwithstanding that at the time the assessment or charge is made he may have left the United Kingdom, if he has so left the United Kingdom for the purpose only of occasional residence abroad.

In the present instance there is no such rule and this appeal must be decided strictly on its facts in relation to the common ordinary meaning of the words "resident" or "ordinarily resident".

The evidence here discloses that the taxpayer's house in Toronto was occupied by the appellant's wife and child until February 1958 when it was sold; at all times from August 2, 1957, until the end of the 1957 taxation year he had a home where he could return at any moment as of right; he in fact returned on three occasions: before going to Europe on a business trip, then on his way back and a few days around Christmas. A car belonging to him but used by his wife, remained in Toronto until the latter's departure; he maintained two bank accounts, one for his mortgage payments on the house in Toronto and the other for his wife's household expenses. On the other hand, in July 1957, he put up his house in Toronto for sale, resigned his membership in a Toronto club, transferred all his personal belongings, clothes and hobbies to Minneapolis, re-applied for and obtained resident membership in his club in Minneapolis, brought his own car back and allowed his wife to stay in Toronto as caretaker for the home and in order to insure its sale.

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The majority of the cases reviewed dealt with taxpayers whose original abode was either in the United Kingdom or Canada and who took up residence in other countries. As pointed out by Taschereau J. in the *Thomson* case at p. 218:

> Moreover in the majority of these cases, the taxpayer was held liable not because his visits to England were of such a nature that they were considered sufficient to qualify him as a "resident", but for the reason that he had never ceased to be a resident of England, and that his occasional absence had never deprived him of the status of British resident.

In the present instance we are dealing with the case of a man whose original residence was in the United States; he was sent to Canada to take charge of a new operation for his company and once the Canadian company was properly set up and running smoothly, he was called back to the parent company to take over new responsibilities and there and then, but for the sale of his house in Toronto, severed himself entirely from Canada.

From the evidence, I am satisfied that the only reason why the appellant's wife and son remained in Toronto until February 1958 was for the sole purpose of insuring the sale of the house and that the retaining of two bank accounts, one for the mortgage payments and the other for his wife's household expenses, as well as the use of one of his cars by his wife, was a logical consequence of the necessary means taken by him to sell his house in Toronto.

The three visits made by the appellant during the period under review were, as far as the Christmas visit is concerned, of such a singular occurrence and as far as the stopovers, of such a transitory and incidental nature, that I fail to see how this could be construed as implying residence in Canada. I would see here the simple gesture of a husband who has changed residence but visits with his family when going through the city where they had to temporarily live.

The circumstances of the present case are somewhat similar to an English decision in re *Rex v. Aldrington, Houghton, and Hove Income Tax Commissioners*[1]. The applicant in this case was the owner of a freehold of No. 4 King's Gardens, Hove, and had in fact resided there until 1907. After that year he had removed to Berkshire; but from 1907 to 1911 he had been regularly assessed to income

[1] [1916] L.J. 1753.

tax under Schedule (A) as owner, as well as to inhabited-house duty as occupier; the house was fully furnished and ready for residence; application for returns of income tax were regularly addressed to the applicant at the address, including the year 1911, and returned duly filled up; in 1913, in making certain affidavits relating to the estate of his deceased wife, the applicant had described himself as of No. 4 King's Gardens, Hove. In reply, the applicant stated that he had never lived at Hove since 1907, and had in that year instructed local agents to sell or let the house furnished, and that the documents referred to in 1913 were filled in by his solicitors. Lord Reading, at p. 1755, in his decision states:

> Upon the evidence I am, however, convinced of the truth of the explanation of the use by the applicant of the address in question, and am satisfied he has not resided there since 1907.

I do feel that the situation here is somewhat similar to the above case and I am convinced of the truth of the reasons why the appellant's wife and son remained in Toronto after the appellant had himself definitely taken residence in Minneapolis, U.S.A.

Had the retention of the house in Toronto and the fact that the appellant's wife and child remained there been indicative of something other than that of wishing to sell the house without sustaining too great a loss, I would be inclined to hold as a matter of fact that the appellant had two residences for taxation purposes, one in Toronto and another in Minneapolis, U.S.A. However, such is not the case, indeed from the evidence it appears that as of August 2, 1957 the house in Toronto became, as far as the appellant is concerned, merely a house to sell and his wife and son remained there for that sole purpose, departing as soon as it was sold.

I therefore feel that the appellant, in this case, has established to my satisfaction that he had on August 2, 1957 divorced himself completely from his residence in Canada and that the fact of his wife and son remaining in Canada until the sale of his house was explained in a satisfactory manner. For the reasons which I have set forth above, I am of the opinion that the appellant must succeed and I therefore find that the appellant did not reside in

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Canada from August 2, 1957 to December 31 of that year and that, therefore, he is entitled to the deductions provided by section 29 of the *Income Tax Act*. Therefore, there will be judgment allowing the appeal and declaring that the appellant is entitled for the year 1957, but from August 2, 1957 only, to the deductions provided by section 29 of the *Income Tax Act*. The appellant is also entitled to the costs of the appeal.

Judgment accordingly.

BETWEEN:

JOSEPH SEDGWICK ..... APPELLANT;

AND

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

1961
June 22, 23
1962
June 28

Revenue—Income Tax Act, R.S.C. 1952, c. 148, s. 6(1)(c)—Partnership—Capital or income—Amount paid for relinquishing right to receive profits of partnership held a capital receipt—Appeal allowed.

In 1949 appellant and four other persons entered into an agreement with one Purcell to lend to Purcell a sum of money with which to purchase a seat on the Toronto Stock Exchange and to provide working capital for a stock brokerage business. The agreement provided for payment to each of the five lenders of a percentage of the annual net profits of the business after an allowance to Purcell and also that they were not to be considered as partners in the business but only as lenders. On the first day of February, 1956 the arrangement was rescinded by an agreement between the lenders and Purcell by which Purcell agreed to pay to the lenders the amount of the loan outstanding, the increase in value of the seat on the Exchange, the share of the lenders in the profits of the business for the fiscal year ending March 31, 1956 and the share of the lenders in the goodwill of the business. The Minister assessed the appellant for tax on his share of the profits of the brokerage business for the 1956 fiscal period. An appeal to the Tax Appeal Board was dismissed and the appellant appealed to this Court. The Court held that the arrangement between the parties was that of a partnership and not merely one involving the lending of money, and that the partnership must be considered as dissolved on February 1, 1956 the date of the agreement rescinding the 1949 agreement.

Held: That the amount paid to appellant for relinquishing his right to receive profits of the partnership was a capital receipt and not income.

APPEAL under the *Income Tax Act.*

The appeal was heard before the Honourable Mr. Justice Ritchie, Deputy Judge of the Court, at Toronto.

Terence Sheard, Q.C. for appellant.

F. J. Cross and *P. M. Troop* for respondent.

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

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RITCHIE, D.J. now (June 28, 1962) delivered the following judgment:

This appeal is from a judgment of the Tax Appeal Board affirming a re-assessment of tax made by the minister, pursuant to the provisions of the *Income Tax Act,* on the appellant's 1956 income. Little, if any, dispute exists respecting the facts involved.

Under date of March 31, 1949 Mr. Sedgwick and four other parties entered into an agreement with one John Edward Purcell who was desirous of purchasing a seat on the Toronto Stock Exchange. In the agreement the appellant and his associates are described as "the lenders" while Purcell is described as "the proposed exchange member". All of the lenders were personal friends of Purcell who had been employed by a brokerage house as a "customer's man".

For the purpose of financing the purchase of the stock exchange seat at a cost not exceeding $38,000.00 and providing working capital for the operation of a stock brokerage business, each lender agreed to advance Purcell $15,000.00 and postpone and subordinate the re-payment of such advance to all debts, liabilities and obligations which might be owing in respect of the operation of the business. The agreement did not provide for the payment of any interest in respect of the advances but, in lieu thereof and in consideration of the advances being made, it was provided that each of the five lenders should be entitled to receive an amount equivalent to eighteen percent of the yearly net profits of the business, to be computed after payment to Purcell of $7,000.00 "for his services in the said brokerage business" and provision for income tax. Purcell was to receive the remaining ten percent of the profits.

As paragraphs 4, 8, 9, 10, 12, 13 and 16 of the agreement appear to have particular relevance to the issue herein, I shall quote them in full, rather than attempt to paraphrase. They are:

> 4. If at any time while the said Brokerage business is in operation additional monies are required pursuant to the regulations of the Toronto Stock Exchange for the operation of the said brokerage business, and a majority of the Lenders agree that it is in the best interests of the said business that additional monies shall be advanced, each Lender shall, in addition to the advances then already made as set out above, advance by way of loan additional monies to the Proposed Exchange Member up to but not exceeding $5,000 on the understanding same shall be repaid pro rata with the other Lenders as soon as expedient, bearing in mind the provisions of the agreement marked "A" hereto annexed.

8. As security for the monies advanced by each Lender hereunder, the Proposed Exchange Member covenants with each Lender to hold the Stock Exchange Seat and such other assets he may acquire from time to time by reason of the operation of the said brokerage business, in trust for the Lenders, their heirs, executors, administrators and assigns, but at all times subject to the provisions of the Agreement "A" hereto annexed. The Proposed Exchange Member doth hereby constitute and appoint a majority of the Lenders, their heirs, executors, administrators and assigns, the true and lawful attorneys of the Proposed Exchange Member to transfer, assign and set over unto the Lenders, their heirs, executors, administrators and assigns, or nominee or nominees, the said Stock Exchange Seat, and all other assets added thereto through the operation of the said brokerage business.

9. Each Lender covenants and agrees with the other Lenders that all and any matters relating to, arising out of, or concerned with this Agreement shall at all times be decided by the decision of a majority of the Lenders, and that once such a decision is given same shall be final and binding on all the Lenders as if it were a unanimous decision of the Lenders. Each Lender agrees with the other Lenders to do all things and execute such documents as may be necessary or useful in order to give full effect to the true intent and meaning of these presents.

10. No Lender may demand repayment from the Proposed Exchange Member of any monies advanced hereunder unless it is the decision of the majority of the Lenders that such demand be made, and then only subject to the provisions of the Agreement marked "A" hereto.

12. The Proposed Exchange Member covenants and agrees with the Lenders as follows:—

(*a*) Not to engage in any other business or venture, nor enter into any transaction or transactions for his separate account which might be entered into for the benefit of the business, except reasonable personal trading with his own private funds.

(*b*) To devote his whole time and attention during customary business hours to the management and conduct of the affairs of the said brokerage business.

(*c*) To act faithfully, honestly and diligently in the performance of his duties and in the interests of the said business.

(*d*) To conduct the business in accordance with good business practice and to only carry on a commission business.

(*e*) To make full disclosure at any time or times when requested so to do by the Lenders of all accounts, books of account and records, and all other matters or things pertaining to the said business and the conduct and operations thereof.

(*f*) To obey the lawful directions of the Lenders or their agent or agents in writing named.

13. The Proposed Exchange Member shall be paid for his services in the said brokerage business, as an expense of the business, the annual sum of $7,000 payable at the rate of approximately $135 weekly and his term of employment shall commence forthwith upon his election as a Member of the Toronto Stock Exchange and upon him devoting his entire time to the organization and/or operation of the said brokerage business, and shall continue in full force and effect until either party hereto terminates same upon 4 weeks' notice in writing to the other.

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Notwithstanding anything herein contained, the Lenders shall have full power hereunder to terminate the employment without notice if the Proposed Exchange Member is guilty of any breaches of any of his covenants hereunder, or is derelict in his duties in any way.

16. Nothing in this agreement contained shall be deemed to constitute the Lenders or any of them as partners in the brokerage business of the Proposed Exchange Member, or to make the Lenders or any of them liable to the creditors of the Proposed Exchange Member, it being agreed between the parties that the liability of the Lenders shall be restricted to the several advances by way of loan hereinbefore provided for.

Schedule A was executed by the lenders, Purcell and the Auditor of the Toronto Stock Exchange. It is a form of subordination agreement approved by the Exchange.

Mr. Sedgwick testified he had no thought of becoming a partner in the Purcell business "either in law or in fact" and, to make that fact abundantly clear, had insisted on the inclusion of paragraph 16 in the agreement. In his view it would be improper for him, as a lawyer whose practice is exclusively that of a barrister, to be a partner in a business of any kind.

While, under the terms of the agreement, the appellant was obligated to advance $15,000.00 to Purcell, he signed the agreement both on his own behalf and as trustee for a friend who did not wish to disclose his interest. His initial advance, accordingly, was only $7,500.00, one-tenth of the $75,000.00 total. Later, pursuant to the above quoted paragraph 4, he advanced additional amounts of $1,250.00 on May 19, 1952 and $2,500.00 in May, 1954 and so brought the total of his advance to $11,250.00, one-tenth of the total which eventually was advanced by the lenders.

Shortly after execution of the agreement Purcell, because of conflict with stock exchange policy, requested that paragraphs 8 and 12 (*f*) be deleted from it. The lenders immediately acquiesced but it was not until March 31, 1953 that each of them addressed a letter to Purcell reading:

I hereby agree that paragraph 8 on page 4 and clause (*f*) of paragraph 12 on page 5 of the original agreement dated March 31st, 1949 should be deleted from the agreement and henceforth should not be regarded as part of the said agreement.

The brokerage business prospered. From 1950 to 1955 inclusive the appellant received as his share of the profits:

1950	$ 3,206.12
1951	7,483.17
1952	8,596.59
1953	10,313.26
1954	5,229.31
1955	13,765.85
	$48,594.30

As he was entitled to one-tenth of the ninety percent share of the profits allocated to the lenders, it would seem the profits of the business, during those six years, ranged from a low of $35,623.56 in 1950 to a high of $152,953.89 in 1955. In the income tax returns filed by Mr. Sedgwick the above amounts were listed as "investment income".

About October 1955 the Stock Exchange management advised Purcell that, commencing January 1, 1956, only persons active in the business of a member house would be permitted to participate in the profits earned by it and that, accordingly, his agreement with the lenders must terminate not later than December 31, 1955. Quite naturally, the lenders were disturbed by the thought of losing a lucrative source of income. During the Christmas season the appellant discussed the situation with the president of the Stock Exchange and sought permission for the agreement to continue in effect. The president told him it was impossible to accede to that request but suggested the Governors might permit the lenders to continue their loans at a fixed rate of interest, not exceeding ten percent, and subject to an approved subordination agreement. Mr. Sedgwick then sought permission to have the agreement remain in effect until March 31, 1956, the end of the current fiscal period of the brokerage business. The president agreed to submit that request to the Board of Governors but they rejected it. The lenders and Purcell then entered into a new agreement under date of February 1, 1956.

Notwithstanding the fact that the lenders had purported to delete paragraph 8 from the former agreement, there is in the 1956 agreement a recital setting out that the stock exchange seat is held by Purcell in trust for the lenders. It also recites:

AND WHEREAS all Parties hereto are content to carry on the business on the terms and conditions it has been carried on in the past, but the Board of Governors of the Toronto Stock Exchange has made a

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ruling that as the Creditors are not actively engaged in the business they can no longer take a share of the net profits of the business as remuneration for the moneys which they have advanced to the business in lieu of a fixed rate of interest.

AND WHEREAS although representation on behalf of the Creditors has been made to the said Board of Governors, protesting against the injustice of such a ruling, nevertheless the said Board of Governors has been adamant and as a result the Parties hereto have no alternative other than to make the arrangements hereinafter set forth if the business is to be carried on, as Purcell is financially unable to pay off the moneys owing to the Creditors and still be in a position to meet the financial requirements of the Toronto Stock Exchange.

The agreement then continues in part:

1. It is mutually agreed:—

(*a*) That to date the advances of money to Purcell by the Creditors amount to ..... $112,500.00.

(*b*) That the increase in the market value of the said seat on the Toronto Stock Exchange is fixed at ..... $ 63,000.00.

(*c*) That the share of the Creditors in the cash surrender value of the insurance policy is hereby fixed at ..... $ 4,850.00.

(*d*) That the share of the Creditors in the net profits of the business for the fiscal year ending March 31st, 1956, is hereby fixed at .... $300,000.00.

(*e*) That the share to which the Creditors are entitled in the good will of the business is hereby fixed at ..... $ 69,650.00.

Total $550,000.00.

2. It is further agreed that the Original Agreement shall be terminated by mutual consent of the Parties hereto for the reasons set out in the third recital hereof, and that the Creditors shall no longer be entitled to share in the net profits of the business. As consideration for the Creditors terminating the Original Agreement and giving up their interest in the Stock Exchange seat, and in the physical assets of the business and their right to share in the profits of the business as aforesaid, Purcell covenants and agrees to pay to each of the Creditors the amount set opposite his name below, totalling in all $550,000.00, payable at the times hereinafter set forth:—

To Joseph Sedgwick	$220,000.00
To Kenneth W. Peacock	$110,000.00
To Isabel Manley	$110,000.00
To Donald George Ewen	$ 55,000.00
To Kenneth Ewen	$ 55,000.00
Total	$550,000.00

Purcell shall pay $150,000.00 on account of the said sum of $550,000.00 by April 15th, 1956 as follows:—

To Joseph Sedgwick	$ 60,000.00
To Kenneth W. Peacock	$ 30,000.00
To Isabel Manley	$ 30,000.00
To Donald George Ewen	$ 15,000.00
To Kenneth Ewen	$ 15,000.00

3. The balance of the said sum of $550,000.00, namely $400,000.00 (hereinafter referred to as "the loan") shall be a loan by the Creditors to Purcell and shall bear interest at the rate of 10% per annum until paid, and interest at the aforesaid rate shall be payable quarter-yearly on the last days of June, September and December in the year 1956 and thereafter on the last days of March, June, September and December in each year until paid.

Paragraphs 5 (*g*), 6 (*b*), (*d*) and (*e*) are, in my view, also of importance. They read:

5. As further consideration for the Creditors terminating the Original Agreement on the terms and conditions set forth above, Purcell covenants and agrees with the Creditors that as long as the loan or any part is outstanding—

(*g*) That in each and every year he will make available to the Creditors for repayment on account of the loan such moneys of the business as the Auditor of the Toronto Stock Exchange consents he may make available, and he shall forthwith upon receiving such consent offer said available moneys to the Creditors as a payment on account of the loan.

6. It is mutually understood and agreed between the Parties as follows:

(*b*) Subject as aforesaid, if at any time moneys are available for repayment of all or any part of the loan, Purcell shall pay out of such funds such moneys as any Creditor is entitled to upon such Creditor making a formal demand for same, despite the fact such Creditor had previously refused to accept same.

(*d*) The loan, or such part as remains unpaid, shall become immediately due and payable upon the happening of any or all of the following events:—If Purcell or his successor in business becomes bankrupt; or if a receiving order is made against him; or if a judgment is obtained and remains unsatisfied for a period of twenty days.

(*e*) Subject to the terms of subsection (*g*) of Paragraph 5 and subsections (*b*) and (*d*) of Paragraph 6 hereof, the said loan of $400,000.00 shall be due six years from the date hereof, but that payment of same will at all times be subject to the terms and conditions of the Subordination Agreement referred to in Paragraph 4 hereof.

While paragraph 2 of the 1956 agreement provides that $220,000 shall be paid to the appellant, it is common ground he, on his own account, was entitled to receive only one-quarter of that amount, i.e., $55,000, being one-tenth of the total consideration. No clear explanation was advanced as to why Mr. Sedgwick is shown as entitled to receive $220,000. There is some suggestion he executed the 1956 agreement in three capacities, on his own behalf, as trustee for the one half share already referred to and as trustee for another full share which had been acquired by another party from one of the original lenders.

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During the year 1956 the appellant received $15,000 on account of his share of the consideration for the lenders entering into the 1956 agreement and also received $2,000 as interest on the $40,000 deferred balance payable to him thereunder. Because he was in England during the month of April 1957, his secretary prepared, signed and filed his 1956 income tax return. Under a heading "All Other Investment Income" there is included an item reading:

Purcell Investment Account (T20 in file of Jack Purcell) $32,000.00.

The notation "T20 in file of Jack Purcell" is hand written and appears to have been inserted by a departmental officer. My impression is there is an intra departmental form bearing the designation T20. The record is silent as to the connection between the T20 form in the file of Jack Purcell and the income tax return of the appellant.

The record also fails to disclose the information which led to inclusion of the $32,000 item in the tax return and how it was computed. Counsel, however, agreed that the amount included a sum of $2,000 received by the appellant in 1956 as interest on the deferred balance of $40,000 owing to him by Purcell. The Crown maintains the remaining $30,000 is the appellant's one-tenth share of the $300,000 allocated to the lenders from the 1956 profits.

The appellant maintains it was through an error his 1956 tax return listed the sum of $32,000 as received from Purcell. He concedes $2,000 of that amount is taxable as an interest receipt but maintains the only further amount he received from Purcell in 1956 was $15,000 which should be regarded as a capital receipt. There can be no doubt that $15,000, plus interest on the $40,000 balance payable to him, is all the appellant, under the terms of the 1956 agreement, could have compelled Purcell to pay him during 1956.

I am satisfied the $32,000 item was included in the appellant's income through an error on the part of someone.

The amount of tax originally assessed in respect of the appellant's 1956 income was increased by an amount of $695.57 through a re-assessment made by the minister on March 5, 1958. Notice of objection to this re-assessment was filed on April 1, 1958. When drawing the objection, the appellant's solicitor took advantage of the opportunity to

object also to inclusion in the 1956 income of the $30,000 item. The re-assessment was confirmed by the minister on February 2, 1959 on the ground that

> the profit from the partnership of Jack Purcell and Company to the extent of $30,120.68 has been properly taken into account in computing the tax payer's income in accordance with the provisions of sections 3 and 4 and paragraph (c) of section 6 of the Act.

The appeal relates to inclusion in the 1956 income of the appellant of $30,189.84 made up of three items of $30,000, $125.68 and $64.16 respectively. Evidence, however, was lead and argument addressed only in respect of the $30,000 item.

The appellant advances two propositions:

1. The payment made and the payments agreed to be made by Purcell under the 1956 agreement, while calculated in respect of probable profits of the brokerage business, are not part of such profits but payment for relinquishment of the right to participate in future profits and for the relinquishment of other rights and, as such, are capital receipts.

2. If the $30,000.00 is income it does not accrue to the appellant as a partner but as a creditor and so only the cash actually received in 1956 should be included in his income for that year.

Three main contentions are advanced on behalf of the minister:

1. Under the 1949 agreement the lenders became partners in the firm of Jack Purcell & Company.

2. The partnership was dissolved by the 1956 agreement.

3. The amount of $300,000.00, designated by the 1956 agreement as "the share of the creditors in the net profits of the business for the fiscal year ending March 31st, 1956", constitutes earnings of the partnership in the 1956 taxation year of the appellant.

The question whether the lenders were creditors or partners of Purcell must, in my view, be determined by the substance of the relationship which was created between them by the 1949 agreement and which was terminated by the 1956 agreement rather than by the form of, or the precise language of any provision contained in, either agreement.

In the eleventh edition of Lindley on *Partnership* the learned authors state at page 50:

> Cases which present most difficulty are those in which persons agree to share profits and losses and at the same time declare that they are not to be partners. The question then arises, what do they really mean? If they have in fact stipulated for all the rights of partners, an agreement that they shall not be partners is a useless protest against the consequences of their real agreement.

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It is apparent that in settling the form of the 1949 agreement the draftsman had regard to rule 3(*d*) contained in section 3 of the *Partnerships Act*, R.S.O. 1960, chapter 288. It is:

> 3. In determining whether a partnership does or does not exist, regard shall be had to the following rules:
>
> 3. The receipt by a person of a share of the profits of a business is prima facie evidence that he is a partner in the business, but the receipt of such a share or payment, contingent on or varying with the profits of a business, does not of itself make him a partner in the business, and in particular,
>
> (*d*) the advance of money by way of loan to a person engaged or about to engage in a business on a contract with that person that the lender is to receive a rate of interest varying with the profits, or is to receive a share of the profits arising from carrying on the business, does not of itself make the lender a partner with the person or persons carrying on the business or liable as such, provided that the contract is in writing and signed by or on behalf of all parties thereto.

A like provision of the English *Partnership Law Amendment Act*, 1865 (28 and 29 Victoria, chapter 86), sometimes referred to as Bovill's Act, was considered in relation to a somewhat similar agreement in *In Re Megevand; ex parte Delhasse*[1]. At page 67 of the Law Journal volume Lord Justice James said:

> If ever there was a case of partnership, this is one. Delhasse has all the essential powers of a partner, right to control the business, and a share of the profits and losses. But it is said that there are words in the agreement which prevent the operation of the contract to which I have referred—words that shew the relation of lender and borrower was intended. The words are a recital of section 1 of Bovill's Act, and a declaration in article 4 of the agreement that Delhasse's advance is by way of loan under that section, and does not, and shall not, be considered to render Delhasse a partner in the business. Now, do those words control the rest? It is clear they do not. The word "loan" is put in, it is true; but looking at all the stipulations, they are utterly inconsistent with a real loan. There is nothing to make the two personally liable in respect of the loan in any circumstances whatever. The loan was not a loan to the two on their personal responsibility, but a loan to the business, which was to be carried on by the two partners for the benefit of all three, and was to be paid out of the business, and that only. The words introduced are a mere sham and contrivance to elude the law of partnership, to call that thing a loan which was not a loan, and to enable a man to be the real and substantial owner of a business, and yet not be liable to losses in case they are incurred.

[1] (1878) 7 Ch. D. 511 (C.A.); 47 L.J. 65; 38 L.T. 106; 26 WR. 338.

And at page 68:

> I am of opinion that the mere putting in of words to the effect that this was a loan under the statute, a loan by one to the others, cannot alter the real transaction. The loan never had any of the real characteristics of a loan, and the agreement was in truth one for a real partnership.

There are at least three respects in which the 1949 agreement is inconsistent with the real characteristics of the relationship of debtor and creditor. They are:

> 1. No maturity date for repayment of the advances is set nor is any provision made for the advances automatically becoming due and payable on the happening of certain specified events.
>
> 2. Paragraph 12 is in terms more usually found in a partnership agreement than to one covering monetary advances. I already have referred to clause (*f*) of this paragraph being deleted from the agreement.
>
> 3. The provisions of paragraph 13, hereinbefore quoted, also are more consistent with a partnership agreement than with one to loan monies to a sole proprietor. The last sentence puts the lenders in the position of being employers of Purcell.

If the lenders really had been loaning money to Purcell the time for, or manner of, repayment of the loans would have been provided for by the terms of the agreement. A minimum provision would have been that in the event of any breach of his covenants by Purcell or in the event of his being derelict in his management duties, the lenders should have the right to declare the amount of their advances to be due and payable and to appoint a receiver-manager for the business.

The 1956 agreement conflicts with the former agreement in several respects and also negatives the relationship of debtor and creditor.

Paragraph 8 of the 1949 agreement, which the lenders purported to delete, declares the stock exchange seat and such other assets as Purcell might acquire through operation of the brokerage business are to be held by him in trust for the lenders as security for the monies advanced by each of them. Notwithstanding the purported deletion of this paragraph, the third recital of the 1956 agreement reads:

> AND WHEREAS while the seat on the Toronto Stock Exchange referred to in the last recital is held in the name of Purcell, same is held in trust by Purcell for and on behalf of the creditors.

That recital contains no suggestion of the seat having been so held only as security for the advances made by the lenders.

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The latter agreement provides Purcell shall pay the lenders $550,000 in consideration of them

(a) terminating the 1949 agreement;

(b) giving up their interest in the stock exchange seat and in the physical assets of the business; and

(c) relinquishing their right to share in the profits of the business.

Included in the computation of the $550,000 consideration are amounts identified with the stock exchange seat, the cash surrender value of a life insurance policy and the good will of the business. All three items are what I am in the habit of referring to as "capital assets". They all come within the language of the paragraph 8 which was supposed to have been deleted from the original agreement.

It is apparent the lenders not only had a right to participate in the profits of the business but also owned an interest in the ownership of the stock exchange seat, the surrender value of an insurance policy (presumably on Purcell's life) and the good will of the business. While the lenders did not intend to incur the liabilities of partners, they did intend to share in the profits of the brokerage business. The application of the monies purported to have been advanced to Purcell was restricted and a right of the lenders to supervise his management of the business was exacted. Any assets acquired either through their "advances" or from the operation of the business were, according to the language of the 1949 agreement, to be held in trust for the appellant and his associates.

As a result of the Stock Exchange ruling the 1949 agreement must be terminated, Purcell agreed to pay the lenders $550,000 in consideration of their agreeing to such termination. The advances totalled only $112,500. A debtor would hardly agree to pay $550,000 in order to satisfy a liability of $112,500.

I find the relationship created by the 1949 agreement between Purcell and the lenders was that of partners rather than that of debtor and creditor.

Section 6(1)(c) of the *Income Tax Act*, R.S.C. 1952, chapter 148 is:

> Without restricting the generality of section 3, there shall be included in computing the income of a taxpayer for a taxation year
>
> (c) the taxpayer's income from a partnership or syndicate for the year whether or not he has withdrawn it during the year.

Despite the reference to "income from a partnership" in section 6(1)(*c*), my finding that the appellant was a partner in the Purcell firm does not necessarily mean the $30,000 item, or any part of it, is taxable as income in his hands.

The appeal must be disposed of on the issue of whether any of the monies, other than interest, payable to the appellant under the terms of the 1956 agreement constitutes income in his hands. That issue, like the question of whether a partnership was created by the 1949 agreement, must be determined by the substance of the transaction as a whole, rather than by the form or wording of the agreement.

Although the appellant testified the Governors of the Stock Exchange insisted the 1949 agreement must be terminated as of December 31, 1955, there is in the 1956 agreement no mention of that date or of any other date on which the original agreement is to terminate. The partnership, therefore, must be taken to have been dissolved as of February 1, 1956, the date of the agreement and two months prior to the termination of the then current fiscal period. From the material in the record, I infer there was no determination of the profits actually earned up to the date of dissolution. Also lacking is any evidence as to the profits of the brokerage business for the full 1956 fiscal period. During his cross-examination of the appellant, counsel for the minister did suggest the 1956 profit was $467,000. Whether that suggestion had any foundation of fact was left to the imagination. The $300,000 share of the profits which the lenders were purportedly allotted certainly has no relation to $467,000.

Prior to execution of the 1956 agreement all the profits of the business had been distributed annually and, in no year, had the share of the lenders in the profits exceeded $137,658.50. The terms of the dissolution agreement did not require Purcell to pay, apart from interest, the lenders more than $150,000 during 1956. At no time was he in a position to withdraw $30,000 from the business as his share of the 1956 profits of the partnership.

In the absence of proof of what profits actually were earned in 1956, I infer the $300,000 is an arbitrary figure agreed upon as an item to be included in the computation

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of the total consideration to be paid the lenders for relinquishing their rights to share in the profits earned by the business in that and subsequent years and for relinquishing their interests in certain partnership assets.

An authority applicable to the main issue herein is *Van Den Berghs, Ltd. v. Clark (Inspector of Taxes)*[1]. In 1908 the V.D.B. company had entered into an elaborate agreement with a Dutch company to regulate their respective activities and to share their respective profits and losses. In 1927, at the request of the Dutch company, the V.D.B. company agreed to terminate the agreement in consideration of the payment to it of £450,000 as "damages". The House of Lords held this payment to be a capital receipt.

Lord McMillan (All E.R. Rep. 887) said:

> Now what were the appellants giving up? They gave up their whole rights under the agreements for thirteen years ahead. These agreements are called in the stated case "pooling agreements", but that is a very inadequate description of them, for they did much more than merely embody a system of pooling and sharing profits. If the appellants were merely receiving in one sum down the aggregate of profits which they would otherwise have received over a series of years the lump sum might be regarded as of the same nature as the ingredients of which it was composed. But even if a payment is measured by annual receipts, it is not necessarily itself an item of income. As Lord Buckmaster pointed out in *Glenboig Union Fireclay Co. v. Inland Revenue Commissioners* (1922 S.C. at p. 115):
>
> > "There is no relation between the measure that is used for the purpose of calculating a particular result and the quality of the figure that is arrived at by means of the test".

A case upon which the appellant relied strongly is *Rutherford v. The Commissioners of Inland Revenue*[2]. There an agreement had beeen entered into under which a retiring partner should receive from the remaining partners:

(1) the sum of £1,500 "in full satisfaction of his whole share and interest in the profits of the firm for the year" ending December 31, 1921;

(2) a further sum of £200 in respect of outstanding accounts; and

(3) further sums "out of the future profits of the business", diminishing from £500 in the first year after his retirement to £100 in the fifth year, payable by quarterly installments in advance.

The court held the £1,500 was not a share of the profits of the business. At page 692 of the T.C. report the Lord President (Clyde) said:

> The sum of £1,500 was made payable to the retiring partner independently of what might turn out to be the profits actually made in the current year, either as a whole, or during that part of it which preceded

[1] [1935] A.C. 431 (H. of L.); 104 L.J. K.B. 345; 19 T.C. 390; [1935] All. E.R. 874.

[2] (1926) 10 T.C. 683; [1926] S.C. 689.

the date of dissolution. It was nothing but the consideration in respect of which the retiring partner gave up any right he might have had in the profits made in that part of the year; and it would have remained a debt due to him by the remaining partners, personally, even if no profits at all had been shown on a balance struck by the remaining partners—whether at the date of dissolution or at the end of the current year.

Lord Blackburn, at page 696 T.C., put it this way:

It so happened that in October, 1921, one of the partners in the firm, Mr. Frank Rutherford, who under the partnership deed was entitled to 18/64ths of the profits, desired to retire, and an agreement was entered into between him on the one hand and the Appellant and the third partner, Mr. John Smith, on the other, as to the terms on which he should do so. It is on the construction of the terms of this agreement that the answer to the question in this case depends. The second clause of the agreement provides that for five years after the dissolution of the partnership on 31st October, 1921, the retiring partner should be entitled to receive annually "out of the future profits of the business" sums which were to diminish gradually from £500 to £100 per annum. The third clause provides that on the execution of the agreement the two partners who were to continue to carry on the business should pay him a sum of £1,500 "in full satisfaction of his whole share in the profits" for the year current at the date of dissolution. There is a marked contrast between the terms of these two clauses in respect that the payments under clause 2 are expressly described as a payment "out of the profits", while the payment under the third clause is a debt payable by the remaining partners irrespective of what might be ascertained eventually to have been the actual value of the retiring partner's share in the profits as at 31st October, 1921, when the agreement was executed. The retiring partner was paid the £1,500 on that date, and it subsequently proved that the share of the profits to which he would have been entitled amounted to less than that sum. The Appellant contends that the £1,500 should be deducted from the ascertained profits of the firm for the period 5th April to 31st October, 1921, before his own share of the profits for that period can be ascertained. The fair construction of the agreement does not appear to me to provide any justification for treating this sum as a charge upon the profits. In my opinion it must be regarded as a price paid to the retiring partner for his share in the profits and a sum for which the remaining partners remained liable irrespective altogether of what the profits of the firm for the year might prove to amount to.

The lenders agreed to the dissolution of the partnership under protest. The amount they stipulated for as the consideration for their agreement was substantial. It is a computation of five items, being:

1. Total advances by the lenders	$112,500.00	or 20.45%
2. Increase in market value of the stock exchange seat	63,000.00	or 11.45%
3. Share in cash surrender value of insurance policy	4,850.00	or .88%
4. Share in net profits of business for 1956 fiscal period	300,000.00	or 54.55%
5. Share in good will	69,650.00	or 12.66%
	$550,000.00	99.99%

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The only item having any relation to income is the amount of $300,000 which constitutes 54.55% of the total consideration. Following the same line of reasoning, only 54.55% of the $15,000 the appellant received from Purcell in 1956 had any relation to income. That relationship does not, *per se*, render it taxable income.

The mechanics involved in dissolving the partnership did not include winding up of the business and distributing the assets among the partners. Purcell, as a sole proprietor, continued the business previously carried on by the partnership. The real effect of the 1956 agreement was that Purcell, for a price of $550,000, purchased the interest of the retiring partners in the partnership. The total consideration could not be paid in cash because, as recited in the agreement, Purcell was

> financially unable to pay off the moneys owing to the creditors and still be in a position to meet the financial requirements of the Toronto Stock Exchange.

The first installment on account of the purchase price was set at $150,000, to be paid by April 15, 1956. Payment of the $400,000 balance, referred to as a loan carrying interest at the rate of 10% per annum, was deferred. No set times were set for payment of any installments on account of the $400,000 balance. Under certain circumstances, payment of the entire balance might be deferred until 1962 and, even then, payment was subject to the terms of a subordination agreement.

I am of opinion the $550,000 consideration was a fixed sum. The fact that in computing it an item of $300,000 associated with profits was included does not affect its character or quality. Nor is the character or quality of the fixed sum consideration affected by the times for payment of any installments on account of the unpaid balance being subject to the approval of the stock exchange auditor and the wish of any lender. I have in mind the dictum of Lord Buckmaster quoted by Lord McMillan in *Van Den Berghs, Ltd. v. Clark (supra)*.

The right of the lenders to receive any share of the 1956 profits was extinguished by the agreement to accept $550,000 in consideration of them relinquishing their interest in the partnership. Purcell then became entitled to

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the 1956 income in full. Any monies received by the appellant, or which he would be entitled to receive, on account of his share of the $550,000 consideration would be a receipt of capital.

In my view the amount of the appellant's 1956 taxable income was $30,000 less than that determined by the re-assessment.

The appeal will be allowed with costs.

Judgment accordingly.

1961

Oct. 2

1962

May 28

BETWEEN:

DONALD QUON ..... APPELLANT;

AND

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

AND BETWEEN:

LEE K. YUEN ..... APPELLANT;

AND

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

Revenue—Income—Income tax—Income or capital gain—Land bought for market garden resold—Other land sales—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e).

The appellant with two others in July 1955 purchased from B for $18,500 forty acres of farm land on the outskirts of Edmonton for the purpose of a market garden. In December one of the purchasers was asked by a real estate agent if he would be willing to sell the land at $2,000 per acre. As a result of this conversation the purchasers decided not to proceed with the garden scheme but simply to hold the land. In October 1956 one of the purchasers died and the following December the survivors accepted an offer of $80,000 for it. In the period between the purchase and sale both appellants with other associates had engaged in several speculative ventures in the purchase and sale of real estate in and about Edmonton. The Minister treated the profit realized on the sale of the B property as income from a business, and, on the appellants' appeal from the assessment, contended that the purpose for which the land was acquired changed after the purchase

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and that, as the sale was made when the appellants were actively trading in land, the profit from the sale should be regarded as made in the course of trading.

Held: That at the time of purchase the appellants had no other purpose in mind than to establish a market garden. When they realized that the land's value made it impractical to operate it as such they made no attempt to sell and it was only after the death of their associate that they accepted the $80,000. In these circumstances there was nothing to characterize their action as trading in land and the profit realized simply represented an enhancement in value on the realization of a capital asset.

2. That it did not follow from the mere fact that the appellants had engaged in transactions of a trading nature in real estate while holding the property in question that the sale thereof must be regarded as a trading transaction rather than a mere realization of value on sale of an investment.

Appeals allowed and assessments varied accordingly.

APPEALS under the *Income Tax Act*.

The appeals were heard before the Honourable Mr. Justice Thurlow at Edmonton.

Gordon S. D. Wright for appellants.

A. J. Irving for respondent.

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

THURLOW J. now (May 28, 1962) delivered the following judgment:

These are appeals from judgments of the Tax Appeal Board[1], dismissing appeals by the appellants from assessments of income tax for the years 1956 and 1957. As the same problem is involved in both cases, the appeals were heard together. The question for determination is whether a profit realized on the sale of certain real estate which I shall refer to as the Buffel property was income for the purposes of the *Income Tax Act* or a capital gain.

The appellant Donald Quon is a chemical engineer and a professor at the University of Alberta. The appellant Lee K. Yuen is a restaurateur. Both appellants live in Edmonton, and prior to the events to be related neither of them had engaged in dealing in real property or been involved in any speculative venture in real estate. Yuen had been brought up in Calgary, where his father operated a market garden, and he had assisted his father and was

[1] (1960) 25 Tax A.B.C. 415, 417; 61 D.T.C. 41, 42.

familiar with that kind of operation. He was acquainted with one Leong Jung, who had operated a market garden in Edmonton for many years prior to 1942, then sold out and gone to China for several years and subsequently returned to Edmonton, where he worked for Yuen as a dish-washer. In 1953 or 1954, Yuen began looking for a suitable parcel of land to establish a market garden, the plan being to acquire the land and have Jung operate the garden initially in a small way on a share basis and later to build and operate greenhouses. With these plans in mind Yuen made a number of inquiries and looked at different parcels of land. It was desirable to establish the operation as near to the market as possible but though there were market gardens within the city of Edmonton, he soon found that it would not be possible or practicable to obtain land for the purpose within the city limits. He contemplated the possibility that the operation might not succeed or might turn out to be impractical and, with that in mind, was looking for a piece of land which, while suitable for a market garden, would also be one from which, if necessary, he could recover his investment. He also arranged for Dr. Quon, the latter's brother, Harry Quon, and Norman Kwong, a professional football player, to take shares in the enterprise. Ultimately, in July, 1955, the four through a real estate agent purchased from one Buffel for $18,500, 40 acres of his farm outside, but adjacent to, the south-western boundary of the city of Edmonton. This land appeared to be suitable for their purpose, and at the time it was well beyond the limits of urban development. In fact, it is still half a mile beyond the nearest area of urban development and beyond a natural obstacle, as well as a University farm, both of which would ordinarily be regarded as likely to retard urban expansion in that direction. The evidence satisfies me that the area was one in which speculators were not interested at that time, though very shortly afterwards, and probably as a result of the holding of public hearings by a Royal Commission enquiring into the problems of metropolitan development of the cities of Edmonton and Calgary, it became an area in which land speculators were very much interested. I am also satisfied that, at the time of the purchase, the four had no purpose in mind for the property other than to establish a market garden and that it was their intention to go ahead with that plan the next year.

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To start this scheme would entail no very large expenditure or risk but would involve drilling a well at a cost of about $600 and acquiring a truck and some gardening equipment in addition to supplies to be used in the operation. In December, 1955, however, Norman Kwong was asked by a real estate agent if he would be willing to sell the land at $2,000 per acre, and soon afterwards, on hearing that Buffel had sold the remainder of his farm for $760 per acre, the four came to the conclusion that the yield to be expected from market gardening would not be commensurate with the value of the land and decided to postpone commencement of their scheme. They were not committed to Jung to use this particular piece of land for the purpose, and it is not surprising that, on hearing of the increased value, they would be reluctant to go ahead and make any such commitment. Yuen continued his search for a suitable piece of land for several years but ultimately gave it up, as Jung was getting on in years and his son, who had been brought from China to help him, was no longer likely to be available.

During 1956, the four received a number of enquiries about the land but made no attempt to sell it. They arranged to have a crop grown on it by Buffel so that the land would not deteriorate but apparently did nothing else with it. In October 1956 Harry Quon died, and in the following December the surviving members of the group accepted an offer of $80,000 for the land and sold it. In making the assessments under appeal the Minister treated the profit realized on the sale as income and the question for determination in these appeals is whether he was right in so doing.

By s. 3 of the *Income Tax Act* the income of a taxpayer for the purposes of Part 1 of the Act is declared to be his income from all sources inside and outside Canada and to include income for the year from *inter alia* all businesses. By s. 4 income from a business is declared to be, subject to the other provisions of Part 1, the profit therefrom for the year and by s. 139(1)(*e*) business is defined as including a profession, calling, trade, manufacture or undertaking of any kind whatsoever and as including an adventure or concern in the nature of trade but not an office or employment.

The Minister's case for including the profit realized on the sale of the land in question in the computation of the appellants' income is that the purchase and sale of the land

constituted a business within the meaning of the statutory definition and that the profit realized on the sale of the land was income from such business.

The test for resolving such an issue is that stated in *Californian Copper Syndicate (Limited and Reduced) v. Harris*[1] where after explaining the distinction between a gain which is assessable to tax as income from a trade and a gain which is not assessable the Lord Justice Clerk said at page 166:

> 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 realizing a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?

At the trial of the appeals, no question was raised as to the credibility of either appellant, and their evidence, along with that of Norman Kwong, satisfies me that this land was purchased for the particular purpose indicated and not in pursuance of a scheme for making profit by selling it. On the facts related, I do not think it could fairly be said that when buying the property the four were engaged in a business of trading in real estate within the ordinary meaning of the word "business", nor do I think the purchase should be regarded as having been made in the course of carrying on a calling, trade or undertaking of any kind or a venture or concern in the nature of trade within the meaning of "business" as extended by the statutory definition.

It was, however, submitted that the purpose for which the land was acquired changed after the purchase had been made, that the sale was made at a time when the appellants were actively trading in land, and that it should, therefore, be regarded as a sale made in the course of such trading and the profit therefrom treated as having arisen from such trading. In order to deal with this submission, it is necessary to relate the further facts brought out in the evidence upon which the contention was based.

In 1954 the appellants with two other associates had purchased certain premises in Edmonton known as the Radio Supply Building for $55,000 paying $25,000 down and financing the balance on a mortgage. This property was leased to a tenant for a term of which some 4½ years remained unexpired and the rental was sufficient to make

[1] (1904) 5 T.C. 159.

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the mortgage payments and afford a reasonable return on their investment. The group held the property until the lease expired in 1958, endeavoured to get the tenant to renew it, held it for some months thereafter while searching for a tenant or purchaser and ultimately sold it late in 1958 for $75,000. It was not suggested that the purchase of this property was anything but an investment.

In the summer of 1956 the appellant Quon was invited to participate with several others in the purchase of a parcel of vacant land known as the McEachern property situated on the outskirts of the city of Edmonton some 2½ miles from the Buffel property. Quon arranged to have the appellant Yuen participate as well and in all 8 persons including the appellants and Harry Quon made the purchase at $52,000, the share of each of the appellants being 10 per cent. while that of the person who had promoted the scheme was 35 per cent. By this time it had become known that values of land on the outskirts of the city were increasing rapidly and the appellants readily conceded that this property was bought as a speculation with a view to making profit by re-selling it. The property was held by the syndicate until 1959 when it was sold for $189,000.

Late in 1956 or early in 1957 the appellants with 5 others also participated in the purchase of 2 lots in Edmonton known as the Barry-Reid property upon which they hoped to erect a building to be leased. Plans for the building were drawn up but the syndicate had difficulty in raising the money to build it and the property was later sold at a small profit. In the meantime it had been used as a parking lot and part of it had ben let to a seed merchant.

In December, 1956, or January, 1957, after receiving the offer of $2,000 per acre for the Buffel property but before it was accepted, the appellant Quon learned that a farm known as the Eastland property consisted of 31 acres situate immediately west of the Buffel farm was for sale at $1,000 per acre and shortly after the sale of the land here in question, he and 9 others including the appellant Yuen proceeded to buy the Eastland property at that price as a speculation looking to re-sale. They had not however disposed of it up to the time of the trial of these appeals.

The appellant Quon also subsequently participated with others in the purchase of what was referred to as the

Berraby (?) property about which no further details were given in evidence but which was also a speculation looking to re-sale.

It is I think apparent from the foregoing that from the time of the purchase of the McEachern property in the summer of 1956, though not before, both of the appellants were engaged in a venture or ventures in trading in real estate. Indeed though Dr. Quon thought it questionable whether the transactions with respect to the Barry-Reid property were in the same category neither of the appellants had any hesitation in conceding that in purchasing and selling the McEachern property and in purchasing the Eastland property they were trading in land. In my opinion however it does not follow from the fact that prior to the sale of the Buffel property the appellants had been involved with different associates in the purchase of the McEachern and Barry-Reid properties in the course of one or more ventures in trading in real estate and the fact that shortly after the sale along with other associates they were involved in another such venture and that Dr. Quon was engaged in still another later on that the profit realized on the sale of the Buffel property must or should be regarded as profit from a business as defined in the statute. The evidence which I have mentioned and which was neither contradicted nor challenged indicates that the appellants were neither engaged in trading nor in a venture in the nature of trade when in 1955 they bought the Buffel property for the purposes of a market gardening operation. Nor were they engaged in trading or in any venture in the nature of trade when they learned of the sale by Buffel of the remainder of his farm at $750 per acre or when in December, 1955 Norman Kwong was asked if he would be willing to sell the land at $2,000 per acre. Accordingly as I view the matter it is only if, because of events which occurred afterwards, the subsequent sale which they made of the property should somehow be regarded as a trading transaction and the profit in question somehow regarded as having arisen therefrom that the profit can be said to be profit from a business within the meaning of the statutory definition. Situations can of course arise wherein a profit realized on a sale of property will be a trading profit notwithstanding the fact that the property has been acquired otherwise than

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in the course of a trading transaction. Thus Croom-Johnston J. said in *Cooksey and Bibbey v. Rednall*[1] at page 519:

> I have no doubt that if there had been evidence here that at some time after the original purchases of a lot of this property these two gentlemen together had gone in for a system of land development with regard to that or part of it, it would have been open to the Commissioners to find that they had turned what had been an investment into the subject-matter of a trading in land. It does not follow necessarily that they would so find, because it may be that the Commissioners would come to the conclusion that the partnership had not traded but was merely realising a capital asset. Everything must depend on the exact circumstances.

In the present case, however, I do not think that anything that occurred had the effect of turning the property into the subject matter of a trading in land. Having learned that the property was more valuable than they had realized when they bought it and having decided that it would be impractical to proceed with the plan to operate a market garden on it, the owners simply held the property, hoping no doubt that it would increase still further in value and without making any final decision as to what they would do about it, but at the same time without putting it on the market or offering it for sale, until the day came when one of the four owners died and thereafter because of the high price that had been suggested and to some extent also because of the fact that it would be necessary to wind up the affairs of the deceased member of the syndicate, they decided to sell and accepted an offer of $80,000 for it. In these circumstances, I see nothing to characterize their action in selling the property as a trading in land and I am satisfied that the profit in question did not arise from any such trading or from a venture in the nature of trade but simply represents an enhancement of value on realization of a capital investment. The profit was therefore not income within the meaning of the statute and should not have been included in the computation of the appellants' income for income tax purposes.

The appeals will therefore be allowed with costs and the assessments varied accordingly.

Judgment accordingly.

[1] (1949) 30 T.C. 514.

BETWEEN:

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

AND

McCORD STREET SITES LIMITED ..RESPONDENT.

1961
Nov. 20

1962
June 25

Revenue—Income—Income Tax Act, R.S.C. 1952, c. 148, ss. 12(1)(a), 14(2)(3), 85(e), 139(1)(w), 2(a) and 125(1)—Bulk sale of a business including stock on hand or so called inventory—Taxability of proceeds from such sale—Deductibility of cost of such inventory—"An outlay or expense . . . made or incurred . . . for the purpose of gaining or producing income . . . from a business"—Deductibility of outlay or expense under s. 12(1)(a)—Duty on taxpayer to open and close out its inventory at the beginning and end of its taxation year—Appeal dismissed.

The respondent, under the name of Consolidated Oka Sand & Gravel Co. Limited, was engaged for many years mainly in the business of dredging sand from two water lots in the Lake of Two-Mountains, which it transported in its own fleet to other leased properties located at Ville LaSalle, in the Parish of Lachine, Quebec, for storage and distribution purpose. It also owned and managed certain revenue-producing properties which it developed on McCord St., in the City of Montreal.

On March 14, 1955, some time prior to the end of its taxation year, by a bulk or slump sale transaction it disposed of its entire sand business, including its name and good will, for $375,000. On the above date the respondent had on hand 40,000 tons of sand which was included in the bulk sale price and for which the purchaser had agreed to pay one dollar a ton. The cost of production was $52,808.90. The Minister of National Revenue, by reassessment, added the $40,000 so received to the Company's taxable income. The Company's appeal against the assessment was maintained by the Tax Appeal Board. The Minister of National Revenue appealed from the said decision. Counsel for the appellant, at the hearing, conceded that the sum of $40,000 in issue constituted a capital receipt, and not profit on the sale of sand, as claimed in the Minister's assessment, but took the position that it was nevertheless taxable on the ground that the production cost of the 40,000 tons amounting to $52,808.90, reduced to the equivalent of its fair market value as provided by s. 14(2), should be charged against the bulk sale proceeds which amounted to $40,000. In order to arrive at the above conclusion, the appellant looked upon the 40,000 tons as inventory the status of which should be determined as of the date immediately preceding the bulk sale to the appellant.

Held: That no part of the receipt from the bulk sale was a receipt from the appellant's business and was not liable to tax. *Frankel Corporation Ltd. v. The Minister of National Revenue* [1959] S.C.R. 713, followed.

2. That the cost of producing the sand which was sold in bulk was an outlay or expense made or incurred by the taxpayer for the purpose of gaining or producing income and was accordingly deductible under s. 12(1)(*a*) of the Act.

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3. That the cost of the 40,000 tons in question having been incurred in the ordinary course of the Company's business it should be deducted only from sales realized in a like manner.

4. That insofar as inventory is concerned the only obligation on the taxpayer is to open and close out its inventory at the beginning and end of its taxation year, and as there was no inventory on hand at the end of the 1955 taxation year, s. 14(2) of the Act would not be applicable.

APPEAL under the *Income Tax Act*.

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

Alfred Tourigny, Q.C. and *Paul Boivin, Q.C.* for appellant.

John N. Turner for respondent.

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

KEARNEY J. now (June 25, 1962) delivered the following judgment:

This is an appeal from a decision of the Tax Appeal Board[1] dated June 21, 1960 allowing the appeal of the respondent and vacating a reassessment wherein the appellant sought to add $40,000 to the gross profit of $50,464.10 reported by the taxpayer for the taxation year 1955 and which the appellant now seeks to have restored.

During the year in question, the respondent, formerly known as Consolidated Oka Sand & Gravel Limited, made a disposition of its entire sand business by way of a bulk sale or slump transaction which, immediately prior to the sale, included 40,000 tons of unsold sand in respect of which it received in the slump transaction one dollar a ton. The issue in this case turns on the manner in which the $40,000 thus received and the costs incurred in producing it should be treated in the determination of the respondent's taxable income for the year.

It was agreed by the parties that the record as constituted before the Tax Appeal Board, including the transcript of argument, should form part of the record in this Court.

Counsel for the respondent called no witnesses but relied on the evidence of Blanche Manning, Lucien Danis, Secre-

[1] 24 Tax A.B.C. 375.

tary and Treasurer respectively of the respondent Company, and Gordon S. Payne, C.A., its auditor, which was adduced before the Tax Appeal Board.

A reverse procedure was followed by the appellant—on whose behalf no witnesses had been heard before the Tax Appeal Board. Before this Court, however, counsel for the appellant called Omer-Georges-S. Vaillancourt, Accountant with the Department of National Revenue, Income Tax Division, and Gordon McHale, C.A.

It is not the facts themselves but the interpretation to be given to them which is in dispute.

The following is a brief history of the respondent company (hereinafter sometimes called "the taxpayer" or "the company") and a summary in chronological order of the main events which are relevant to the instant issue.

The company was incorporated by Letters Patent of the Province of Quebec under the name of "Oka Sand & Gravel Co. Limited". During the first few years of its existence it acquired a property in the city of Montreal, just off McCord Street, close to a shipping basin abutting the Lachine Canal, where it stored and disposed of sand which it had pumped and transported by its own equipment and marine fleet from the Lake of Two Mountains, in the neighbourhood of the Town of Oka. The respondent possessed deep water lots in the Lake of Two Mountains which it leased from the Minister of Hydraulic & Resources of the Province of Quebec and where it also held a mining concession, covering certain lots forming part of the said lake, in virtue of a grant issued by the Minister of Colonization and Mines of the Province of Quebec.

In 1928, Oka Sand & Gravel Co. Ltd. merged with a company called "Consolidated Sand" and these two companies were absorbed by a new company called "Consolidated Oka Sand & Gravel Co. Limited".

While retaining its McCord Street property, which had large storage facilities and on which the respondent had later constructed a garage and a commercial building from which it was in receipt of rentals, it decided to move its sand business to Ville LaSalle, in the Parish of Lachine, where it leased a property on St. Patrick Street from Raymond Marroni, and certain further contiguous lands from the Minister of Transport and on which it later

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constructed, *inter alia,* an office building. Both of these above-mentioned properties were located on or near the Lachine Canal. The respondent continued to operate its sand business through the medium of its Ville LaSalle and the Lake of Two Mountains properties, and the McCord Street property became a real estate investment from which gross profits—which are not in issue—were realized.

As appears by Exs. A-1 and A-2 filed before the Tax Appeal Board, one Raymond Miron, acting for and on behalf of Oka Sand & Gravel Inc., a company in the process of being incorporated, made in two separate documents a conditional offer to purchase as a going concern the entire sand business of the respondent company, with the exception of its property located on McCord Street for a total consideration of $375,000.

By Ex. A-1 Mr. Miron offered $27,000 for all the respondent's interests relating to its Ville LaSalle and Lake of Two Mountains properties and appurtenances upon its simultaneous acceptance of a second offer (Ex. A-2), wherein he offered to purchase the respondent's marine vessels and accessories for $308,000, payable $158,000 upon the signature of the deed and $150,000 by promissory note falling due six months from the signing of the deed and secured by a statutory mortgage in favour of the vendor on the said marine vessels. Exhibit A-1, *inter alia,* required that the respondent undertake to change its name so as not to include any of the words "Oka", "Sand" and/or "Gravel" and to permit the purchaser to cause to be incorporated a company to be known as "Oka Sand & Gravel Inc." The offer also states that in the event of its acceptance the purchaser shall purchase all the vendors' stock of sand on the leased premises at Ville LaSalle at a price of one dollar a ton. The quantity thereof was to be determined by the certificate of a surveyor acceptable to both parties, but, as appears later, this became unnecessary.

On March 10, by-laws were passed at a meeting of directors of the company and ratified at subsequent meetings of its shareholders whereby the offers contained in Exs. A-1 and A-2 were accepted and two of the respondent's officers were authorized to sign the necessary deeds of sale, and, at the same meetings, appropriate by-laws were passed to have the name of the respondent changed to McCord Street Sites Limited (see Exs. A-3 and A-4).

By March 14, 1955 Oka Sand & Gravel Inc. had been incorporated but apparently the Letters Patent authorizing the change of name of the respondent had not yet been issued. Two deeds of sale, on the above date, were executed (see Exs. A-5 and A-6) between Consolidated Oka Sand & Gravel Co. Ltd. as vendor to Oka Sand & Gravel Co. Inc. as purchaser. As appears in Ex. A-5, which I might call "the offer for Ville LaSalle and Lake of Two Mountains properties", the parties waived the necessity for a future survey and agreed that the quantity of sand on hand at that date should be considered as consisting of 40,000 tons. As a consequence, on the signing of the deed, apart from receiving $27,000 for its Ville LaSalle and Lake of Two Mountains assets of the company, the latter received $40,000 for the sand then on hand. In short, the respondent, for the assets mentioned in Ex. 5 received on its execution the sum of $67,000 and the purchaser undertook to fulfill the obligations of the respondent under the leases included in the sale.

All the prior conditions having been fulfilled, the down payment of $158,000 was made and the transfer of the respondent's marine fleet was effected, thus completing the bulk sale of its entire sand business. Thereafter the only portion of the business previously carried on by the respondent which it retained and continued, after March 14, 1955, to operate, consisted in the ownership and administration of its property and buildings located on McCord Street and from which it derived rentals, which, in 1955, amounted to $16,737 (see statement of operations filed at the instant hearing by Mr. Vaillancourt as Ex. A).

It is admitted by the parties that s. 85(*e*) of the Act, whereby it is provided, *inter alia,* that the sale of an inventory shall be deemed to have been sold in course of carrying on a taxpayer's business missed by a narrow margin being applicable to the bulk sale effected, in the present case, on March 14, 1955, since it applies only to sales made after April 5, 1955. It would appear, indeed, that, when on September 19, 1955 the respondent filed its original income tax return for its taxation year terminating on April 30, 1955, it was under the impression that s. 85(*e*) had been

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made applicable as of January 1, 1955; hence the variations in the respondent's tax return, as mentioned in paragraphs 1 and 2 of the notice of appeal.

Legally speaking, the estimates of his taxable income made by a taxpayer in form T-2 return is of little or no concern. On the contrary, the Minister's reassessment of such return and the validity of the objections thereto, relied upon by the taxpayer, are of the utmost importance. While taking exception to the reassessment of its taxable income made by the Minister, amounting to $90,464.10, the taxpayer acknowledges that it amounted to $50,464.10 (see Ex. A-7, dated April 19, 1960, filed by Mr. Payne; also Ex. A, a comparative statement, dated November 16, 1961, prepared by Mr. Vaillancourt). It follows, therefore, that $40,000, being the difference between the two above-mentioned figures, constitutes the only amount in dispute.

The appellant has also altered the position which he originally adopted. As appears at page 2 of the reassessment referred to in his notice of appeal, the $40,000 in issue was added as "profit on the sale of sand" included in the slump sale in question. In his argument, as I understood it, counsel for the appellant submitted that the Minister no longer seeks to tax the said $40,000 as a sale, because, for reasons which I shall refer to later, he acknowledges that it should be regarded as a capital receipt. Instead, he takes the position that the said $40,000 being the proceeds from an inventory sold as part of its business should serve to cancel out *pro tanto* the costs incurred by the taxpayer in respect of all the sand extracted in the course of its business during 1955.

Briefly, it is said for the respondent that the appellant is endeavouring to impose a tax indirectly which he is prevented by legal precedents from imposing directly.

Mr. Vaillancourt produced as Exhibit A a comparative statement of operations for the year ended April 30, 1955, purporting to show the appellant's computation on one side of the sheet and the respondent's on the other. As mentioned previously, the gross profit derived in the form of

rents from the McCord Street property, as set out in the said exhibit, can be disregarded and the exhibit need not be considered beyond the point were the Department's figures show taxable income or gross revenue from the sand business at $90,464.10 and where a corresponding figure shown by the taxpayer amounts to $50,464.10.

Mr. Payne filed as Exhibit 7 an explanatory computation in support of the figure of $50,464.10 which I propose to make use of, as it shows more clearly than Ex. A how the item of $50,464.10 was arrived at.

Mr. McHale filed as Ex. B a letter which sets out his opinion and reasons for agreeing in principle with Mr. Vaillancourt's conclusion.

The following extracts from Exs. A, A-7 and B, I think, are sufficiently inclusive to bring into relief the conflicting views of the parties.

Statement of Operations for the year ended April 30, 1955
Appellant's Figures
Exhibit A

Sales[1]			$305,803.71
Cost of Sand			
Inventory of sand April 30, 1954		$ 15,562.28	
Cost of sand extracted in 1955		$239,777.33	
Cost of sand sold during 1955[2]		$255,339.61	
deduct: cost of sand sold in bulk	$52,808.09		
less: reduction to market value	$12,808.09		
Market value of sand sold in bulk		$ 40,000.00	
Gross profit			$215,339.61
			$ 90.464.10

[1] Does not include $40,000 received on bulk sale.
[2] Includes cost of sand sold in bulk.

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RESPONDENT'S FIGURES

EXHIBIT A-7

McCORD STREET SITES LIMITED

(formerly Consolidated Oka Sand & Gravel Co. Limited)

1955 Income Tax Appeal

Outline of Taxpayer's Contention

If the sale of the sand business had occurred after Section 85E became effective, the figures would have been as follows:—

Sales during operation of the sand business	$305,803.71	
"Slump" sale of inventory	40,000.00	
Total Sales of Sand	$345,803.71	
Cost of Sand		
Inventory April 30, 1954	$ 15,562.28	
Cost of Sand Produced	239,777.33	
	$255,339.61	
Inventory, April 30, 1955	nil	$255,339.61
Gross Profit as it would be if Section 85E were in effect		$ 90,464.10

But as Section 85E was not in effect, we eliminate the $40,000 from the calculation, on the grounds that no "part of the receipts from the sale was a receipt from the taxpayer's business", so that the Gross Profit (profit before deducting operating expenses) on which the taxpayer claimed to be taxable, is as follows:

Sales while in the sand business		$305,803.71
Cost of Sand		
Inventory April 30, 1954	$ 15,562.29	
Cost of Sand Produced	239,777.33	
	$255,339.61	
Inventory, April 30, 1955	nil	$255,339.61
Gross Profit reported by taxpayer		$ 50,464.10

Mr. McHale, in his letter of November 17, 1961 (Ex. B), addressed to counsel for the appellant, stated in part:

> You have asked me to express an opinion on the accounting principles followed in preparing the financial statements of the above company for its year ended 30th April 1955.
>
> It is a basic and generally accepted accounting principle that in order to determine the profit arising from any transaction, the cost of the items sold must be matched against the proceeds of sale. This is true whether the transaction is of a capital or a revenue nature.
>
> * * *

The profit arising from the normal sales of the company would therefore be as follows:

Sales		$305,803.71
Cost of sales—inventory April 1, 1954	$ 15,562.28	
Cost of production	239,777.33	
	$255,339.61	
Less: cost of inventory on hand 14th March 1955, i.e. immediately before the bulk sale	52,808.09	202,531.52
Profit arising in normal course of business		$103,272.19
Less: reduction to market value as required by s. 14(2) of the Income Tax Act		12,808.09
Profit as determined by the Tax Department		$ 90,464.10

However, when we examine the accounts of the company, we find that against the proceeds of sales in the normal course of business (166,874 tons) were charged the costs of extraction of 210,384 tons, while against the proceeds of the bulk sale (43,510 tons) were charged no costs whatever. In my opinion, costs of $52,808.09 should be charged against the bulk sales proceeds of $40,000.

When it happens, as in a case like this, that by a fiction of law something which clearly constituted stock-in-trade, without undergoing any physical change, suddenly becomes a capital asset, I believe such an occurrence is almost bound to create anomalies insofar as generally accepted accountancy practice is concerned.

Even if it were taken for granted that Mr. McHale's method of computation is more in accordance with good commercial accounting practice than the one adopted by the respondent, this would not put an end to the issue. In my opinion, usually accepted accounting principles must give way to unusual situations, more particularly when they arise not only from the statutory provisions of the *Income Tax Act* but from the dictates of jurisprudence as well. In comparing the two methods of computation, it should be borne in mind, I think, that where income tax is concerned it is the law and not accounting practice which must prevail.

It is important to note that the parties agree that for the year ended April 30, 1955, the respondent's sales amounted to $305,803.71 and both have excluded therefrom the sum of $40,000 received as a result of the bulk sale. One does not have to seek far for the reason which

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prompted this exclusion; it is to be found in the judgment of our Supreme Court in *Frankel Corporation Ltd.* and *The Minister of National Revenue*[1], a case concerned with the effect of a bulk sale made in 1952 which in many respects is similar to the instant one. Martland J., at pp. 725 and 726, set out a long extract from the judgment of the learned trial judge (Thurlow J.) which contains the latter's reasons for reaching the following conclusions:

> . . . . It follows, in my opinion, that no part of the receipts from this sale was a receipt from the appellant's business.

At the bottom of page 726, Martland J. makes the following statement:

> I agree with these conclusions. In my opinion the evidence establishes: (1) that the appellant ceased its trading in non-ferrous metals by December 31, 1951; and (2) that the sale of the inventory of non-ferrous metals as a part of the assets sold by the agreement of December 19, 1951, by the appellant to Federated was not a sale in the business of the appellant, but was made as a part of a sale of a business of the appellant, and consequently the proceeds of that sale were not income from a business within the meaning of s. 4 of the *Income Tax Act*.

Having previously stated at p. 723 that "Section 85E of the Act had no application to this case, as it became effective in respect of sales made after April 5, 1955, Mr. Justice Martland at p. 728 observed:

> . . . . The issue here is not as to what amount should be deemed to be received by the appellant for those goods, but whether the actual amount received was income from the appellant's business, ...

It is of some significance, I think, that here, like in the *Frankel* case, s. 85(*e*) had not come into effect; yet, as appears by Ex. A-7, the appellant's computed figure of $90,464.10 is exactly the same as if it did apply.

To avoid unnecessary confusion, I will here add a comment on the following discrepancy in the figures presented on behalf of the respective parties.

It appears from the exhibits and evidence adduced before the Tax Appeal Board that the parties used the figure of 40,000 tons and $40,000. Mr. McHale, whose evidence was first heard before this Court, makes use of the figure "43,510 tons" while retaining the figure of $40,000. I do not know how this arose. It may be that one set of figures was based on estimate and the other after the sand had

[1] [1959] S.C.R. 713.

been surveyed; but, because of the conclusion I have reached, any discrepancy in calculation resulting therefrom cannot, in my opinion, affect the issue.

It is worth noting, however, that other computations made in the appellant's Exhibits A and B differ somewhat *inter se* and both are radically different in respect of treatment of "inventory" from what is found in the respondent's Exhibit 7. Mr. Vaillancourt, in his report, has added back the figure of $40,000, being the proceeds of the bulk sale, under the title of "Market value of sand sold in bulk". In Exhibit B, Mr. McHale, except by way of comment, makes no mention of the sum of $40,000 but both witnesses regard the 40,000 tons of sand as inventory which should be made subject to s. 14(2) of the Act; it provides:

> For the purpose of computing income, the property described in an inventory shall be valued at its cost to the taxpayer or its fair market value, whichever is lower, or in such other manner as may be permitted by regulation.

In doing so Mr. McHale mentions that he is giving effect to s. 14(2) as of March 14, 1955, but before the bulk sale. No such mention appears in the Vaillancourt statement.

I might here interject that I doubt very much whether the appellant was justified in adopting an unmistakeable slump sale, at one dollar or less a ton, and far below cost, as being synonymous with or a proper criterion for determining the fair market value of the goods in question. However, because of the conclusions I have reached on other grounds, this point is of no importance and may be disregarded.

In Exhibit 7 Mr. Payne, because the company's taxable year ended on April 30, 1955, at which date it had no inventory, inserts a "nil" report in respect of it. Moreover, it is his opinion that, since the $52,808.09 was expended in order to gain income within the meaning of s. 12(1)(*a*) of the Act and although it never attained its purpose, this amount of $52,808.09 should be charged against $305,803.71 and not against the bulk sale proceeds, which he eliminates from his calculation on the grounds that "no part of the receipts from the sale was a receipt from the taxpayer's business".

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Let us first consider whether in law and in fact it can be said that the expenditure in question was for the purpose of gaining income? Section 12(1)(*a*) of the *Income Tax Act*, R.S.C. 1952, c. 148, states:

> 12. (1) In computing income, no deduction shall be made in respect of
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer.

That the answer must be in the affirmative, in my opinion, is self-evident, because during years and years the company had been making identical expenditures for no other purpose and by March 14, 1955 the entire amount of $52,808.09 had been expended.

I think a reasonable conclusion to be drawn from the evidence is that, had the taxpayer foreseen that the sand in question was destined to be sold in a slump sale at a considerable loss, the expenditure made in extracting it would never have been incurred.

A recent decision of our Court in respect of s. 12(1)(*a*) is that of Cameron J. in *Wilson* and *The Minister of National Revenue*[1] at page 217:

> . . . . it is not now necessary to establish that the expense was made or incurred for the purpose of earning the income of the year in which it was made or incurred. It is sufficient to show that it was made for the purpose of gaining or producing income from the business.

Mr. Justice Cameron refers to a statement of the President of this Court, which is found in *The Royal Trust Co.* and *The Minister of National Revenue*[2], reading thus:

> The essential limitation in the exception expressed in Section 12(1)(*a*) is that the outlay or expense should have been made by the taxpayer "for the purpose" of gaining or producing income "from the business". It is the purpose of the outlay or expense that is emphasized but the purpose must be that of gaining or producing income "from the business" in which the taxpayer is engaged. If these conditions are met the fact that there may be no resulting income does not prevent the deductibility of the amount of the outlay or expense. Thus, in a case under the *Income Tax Act* if an outlay or expense is made or incurred by a taxpayer in accordance with the principles of commercial trading or accepted business practice and it is made or incurred for the purpose of gaining or producing income from his business its amount is deductible for income tax purposes.

I consider that the cost of the 40,000 tons in question, which was incurred in the course of the company's business, should be deducted from sales realized in the same manner.

[1] [1960] Ex. C.R. 205.

[2] [1957] C.T.C. 32 at 44.

Because the proceeds of the slump sale do not fall into the above-mentioned category, and for reasons immediately following, such proceeds, in my opinion, should not be charged against the cost of said tonnage.

With respect to the question of inventory, it can be said, I think, that the difference, amounting to $40,000, between the appellant's and respondent's figures of taxable income arises because the appellant, while admitting that the slump sale receipt of $40,000 must be eliminated from the company's profit and loss account, considers that it ought to be brought into and taken into consideration as inventory and applied against the cost thereof as of March 14, 1955.

The respondent, on the other hand, submits that the Minister, in effect, is attempting to disallow a sum of $40,000 (costs amounting to $52,808.09, scaled down by $12,808.09, as required by s. 14(2) of the Act) (*supra*) which is non-taxable as a receipt, by erroneously treating the status of "inventory" as of March 14 instead of April 30, 1955.

On a strict interpretation of the following relevant provisions of the Act, which I think is the only appropriate one in the circumstances, I believe the status of inventory should be determined as of the last day of the company's fiscal year.

Nowhere in the Act is there a provision requiring a taxpayer, under any circumstances, to report his inventory prior to the end of his fiscal year.

Section 4 states that, "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.

Section 139(2)(*a*) of the Act defines "Taxation Year" as follows:

> (2) For the purpose of this Act, a "taxation year" is
> (*a*) in the case of a corporation, a fiscal period, . . .

When s-s. (3) was added to s. 14 by Statutes of Canada 1959, c. 45, it continued to speak of a "taxation year":

> 14. (3) Notwithstanding subsection (2), for the purpose of computing income *for a taxation year* the property described in an inventory at the commencement of the year shall be valued at the same amount as the amount at which it was valued at the end of the immediately preceding year for the purpose of computing income for that preceding year. (Italics are mine.)

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Turning to s. 139, s-s. (1), para. (*w*), we find that "inventory" is defined as follows:

> (*w*) "inventory" means a description of property the cost or value of which is relevant in computing a taxpayer's income from a business *for a taxation year;* (Italics are mine.)

Subsection (1) of s. 125, which speaks of books and records, states:

> 125. (1) Every person carrying on business and every person who is required, by or pursuant to this Act, to pay or collect taxes or other amounts shall keep records and books of account (including *an annual inventory* kept in prescribed manner) at his place of business or residence in Canada . . . . (Italics are mine.)

I think that the foregoing statutory provisions (to which no exceptions are to be found in the Act) make it clear that, insofar as inventory is concerned, the only obligation which rested on the respondent was to open and close out its inventory at the beginning and at the end of its taxation year 1955, and, in my opinion, the evidence undoubtedly shows the respondent, in this respect, fully complied with the Act. I might add that in the *Frankel* case (*supra*), at page 727, it was submitted on behalf of the Minister as an alternative argument

> . . . . that, even if the sale of the inventory of non-ferrous metals was a part of the sale of a business, nevertheless, to effect such sale, such inventory was removed or "diverted" from the appellant's stock-in-trade *before* it was sold and such removal or diversion required that there be placed in the appellant's trading account the market value of the goods so sold, thus giving rise to a trading receipt equal to the amount realized upon such sale. (Italics are mine).

In other words, the Minister (who was respondent in the above case) in effect was seeking to remove the inventory of non-ferrous metals from stock-in-trade and bring it back as a closing inventory as of the moment before it was sold. But Mr. Justice Martland, at page 728, held that "the contention of the respondent on this point also fails".

It is admitted that we are here dealing with an exceptional type of case and one which, in my opinion, was not envisaged taxwise until s. 85(*e*) was introduced into the Act. Because of the *Frankel* case, as I interpret it, and on a strict reading of the provisions of the Act previously referred to, I think it can be said the respondent has successfully discharged the burden of establishing that the reassessment in

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question, as made by the appellant, is unjustified and that the respondent's taxable income should be reduced by $40,000.

I would, therefore, dismiss the appeal with costs and refer the record back to the Minister for reassessment accordingly.

Judgment accordingly.

1960

June 2

1962

May 22

July 31

BETWEEN:

WILLIAMS BROTHERS CANADA LIMITED ..... APPELLANT;

AND

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

Revenue—Income tax—Income Tax Act, R.S.C. 1952, c. 148, ss. 12(1)(a) and 12(1)(b)—Deductibility of cost of acquiring a construction contract by a contractor—Outlay or expense on account of capital or outlay or expense for purpose of gaining income—Appeal allowed.

Appellant was incorporated for the purpose of constructing pipe lines as a contractor. It acquired the interest of Canadian Pipe Line Construction Co. Ltd. in a joint venture together with some equipment at a total cost of $325,000. The equipment was valued at $95,000 and the Court found that the sum of $230,000 had been paid for the acquisition of the contract to do the construction work. The appellant completed the work called for and in its income tax return for the taxation year deducted the payment of $230,000 to Canadian Pipe Line Construction Co. Ltd. The respondent disallowed the deduction and re-assessed the appellant accordingly. On appeal to this Court the respondent contends that the payment constituted an outlay or expense on account of capital and was therefore barred by ss. 12(1)(*a*) and 12(1)(*b*) of the *Income Tax Act*, and, alternatively, that the appellant had not merely bought a construction contract but had actually purchased an interest in a joint venture or partnership which should be considered as a capital asset.

Held: That the $230,000 was laid out for the purpose of earning the income within the meaning of s. 12(1)(*a*) of the *Income Tax Act* since appellant, a pipe line contractor, in order to earn a profit must first acquire construction contracts before it would be able to complete contracts profitably by performing the work.

2. That no asset or advantage of an "enduring" nature was acquired by appellant and so the deduction was not barred by s. 12(1)(*b*) of the Act.

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3. That the acquisition of an interest in a joint venture by a construction company was not the acquisition of a capital asset because the construction company was in the business of acquiring such interests.

APPEAL under the *Income Tax Act*.

The appeal was heard before the Honourable Mr. Justice Cattanach at Ottawa.*

W. E. P. DeRoche, Q.C. and *J. B. Tinker* for appellant.

R. N. Starr, Q.C. and *P. M. Troop* for respondent.

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

CATTANACH J. now (July 31, 1962) delivered the following judgment:

* The appeal was originally heard before the Honourable Mr. Justice Fournier who died without rendering a decision and re-heard before the Honourable Mr. Justice Cattanach. Counsel shown appeared at both or either of the hearings.

This is an appeal against the appellant's income tax assessment for the taxation year ending April 30, 1953.

The appellant was incorporated under Part I of the Companies Act 1934 by letters patent dated April 5, 1949 under the name of Dokken Pipe Line Construction Limited, which name was changed to that of Williams Brothers Corp. (Canada) Ltd. by Supplementary Letters Patent dated April 26, 1950. By further Supplementary Letters Patent dated December 2, 1959, the corporate name was changed to Williams Brothers Canada Ltd., its present style. The purposes and objects of the appellant are to construct pipe lines as a contractor.

During the year 1952 Trans-Northern Pipeline was incorporated for the purpose of causing to be constructed and to operate a products pipe line from Montreal, Quebec, to Hamilton, Ontario, with a branch line from Farran's Point, Ontario, to Ottawa, Ontario, a total distance of approximately 411 miles. There was considerable competition among pipe line contractors, both Canadian and foreign, to obtain contracts for the building of these lines. The appellant was one of the unsuccessful competitors, the contract being granted to a "joint venture" comprised of Mannix Ltd. and Canadian Pipe Line Construction Co. Ltd.

The particulars of the joint venture between Mannix Ltd. and Canadian Pipe Line Construction Co Ltd. are set out in an agreement dated October 1, 1951, filed in evidence as Document 1 of Exhibit 1, and are substantially that the parties to the joint venture shall enter into a construction contract with Trans-Northern Pipeline Company as joint contractors, that all interest in the property and equipment of the venture and on the profits derived from the contract and all contributions to working capital and all possible losses shall be equally shared. It was further provided that the joint venture should be known as Mannix Canadian Pipe Line Construction Company, hereinafter referred to as Mannix Canadian.

The contract between Trans-Northern Pipeline Company and the parties to the joint venture was executed on March 31, 1952, which contract was filed in evidence as Document 2 of Exhibit 1.

Three subcontracts, each dated March 31, 1952, were then entered into by Mannix Canadian, the first with Mannix Ltd., the second with Canadian Pipe Line Construction Co. Ltd. and the third with Sparling-Davis Company Limited for the construction of their respective portions of the pipe line. Subsequently, Mannix Ltd. subcontracted a portion of the work called for by its subcontract to the appellant and Mannix Canadian subcontracted to the appellant two river crossings which had not been previously subcontracted.

The appellant, when first incorporated, enjoyed only moderate success. Subsequently, the appellant became a wholly owned subsidiary of Williams Brothers Company incorporated under the laws of the State of Nevada and then began a more aggressive policy to obtain pipe line construction work. The present pipe line was the first work of major proportions which the appellant was in a position to undertake. Having been unsuccessful in obtaining a contract to construct the pipe line as prime contractor and being desirous of obtaining a still greater portion of the work than called for by its subcontracts with Mannix Ltd. and Mannix Canadian, the appellant agreed to accept from Canadian Pipe Line Construction Co. Ltd. an assignment of all "rights, title and interest in and to that agreement between Trans-Northern Pipeline Company and Mannix

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Ltd. and ourselves as contractors", that is to say in the agreement dated March 31, 1952 and filed as Document 2 of Exhibit 1 and in addition undertook the obligations and benefits of the subcontracts, both dated March 31, 1952, filed as Documents 3 and 4 of Exhibit 1, between Canadian Pipe Line Construction Co. Ltd. and Mannix Canadian. In short, the appellant by virtue of this agreement stands precisely in the shoes of Canadian Pipe Line Construction Co. Ltd. The consideration for the assignment and the sale of certain equipment was $325,000. This agreement was confirmed by a letter dated April 3, 1952, from Canadian Pipe Line Construction Co. Ltd. to the appellant, filed as Document 8 of Exhibit 1. Attached to the letter was an agreement respecting the sale of equipment which was for a consideration of $95,000. By subtraction therefore, the consideration for the assignment of the interest of Canadian Pipe Line Construction Co. Ltd. in its contract with Trans-Northern Pipeline Co. and its subcontracts was $230,000.

The foregoing arrangements were embodied in an agreement dated April 30, 1952, filed as Document 9 of Exhibit 1, between Canadian Pipe Line Construction Co. Ltd., the appellant, Mannix Ltd. and Trans-Northern Pipeline Company whereby the interest of Canadian Pipe Line Construction Co. Ltd. in the principal contract and in the subcontracts was assigned to the appellant and Trans-Northern Pipeline Company and Mannix Ltd. consented to such assignment.

The appellant completed the work called for in its subcontracts in its taxation year ending April 30, 1953, as did the other subcontractors.

The appellant filed its income tax return for its taxation year but in computing the tax payable, the appellant deducted the payment of $230,000 to Canadian Pipe Line Construction Co. Ltd. for the assignment, as an expense incurred for the purpose of gaining or producing income.

By notice of re-assessment dated November 17, 1953, the respondent disallowed the deduction of $230,000 as an expense.

On November 15, 1954, the appellant filed a Notice of Objection to the Re-assessment under section 58 of the *Income Tax Act,* 1952 R.S.C. c. 148, and by notification

dated May 30, 1955, the respondent confirmed the assessment on the ground that the amount of $230,000 paid to Canadian Pipe Line Construction Co. Ltd. claimed as a deduction from income was not an outlay or expense incurred by the taxpayer for the purpose of gaining or producing income within the meaning of paragraph (*a*) of subsection (1) of section 12 of the *Income Tax Act,* but was a capital outlay within the meaning of paragraph (*b*) of the said subsection (1) of section 12.

It is from this assessment that an appeal is brought to this Court.

The appeal, therefore, involves consideration of sections 12(1)(*a*) and 12(1)(*b*) of the *Income Tax Act* which provides as follows:

> 12. (1) In computing income, no deduction shall be made in respect of
>
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer,
>
> (*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part.

The issue in the appeal is whether the payment of $230,000 made by the appellant to Canadian Pipe Line Construction Co. Ltd., in the circumstances described above, constitutes an outlay or expense made or incurred by it for the purpose of gaining or producing income from its business within the meaning of the exception expressed in section 12(1)(*a*) of the Act and is therefore outside the prohibition of the section, as contended by the appellant, or whether the said payment was a capital outlay within the meaning of section 12(1)(*b*) and accordingly is not properly deductible in computing income, as contended by the respondent.

The appellant was in the business of pipe line construction as contractor which means that it was not a seller of goods but its function is merely to put the pipe into the ground and it is from this work any profit is derived. Therefore, to earn a profit the appellant must do two things, first it must get the job and secondly it must complete the job and it follows that expenditures made for the purpose of getting the job would be an outlay or expense made or

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incurred by the taxpayer for the purpose of gaining income from the business of the taxpayer, (if not otherwise prohibited by the Act).

The evidence discloses that pipe line construction jobs are obtained in a variety of ways, first by contract with the owner, which in the present case the appellant attempted to do but was unsuccessful or secondly by way of subcontracts of various types.

The evidence also discloses that joint ventures or syndicate arrangements such as entered into between Mannix Ltd. and Canadian Pipe Line Construction Co. Ltd. are commonplace in the business of constructing pipe lines and are accordingly an accepted method of business practice in this particular trade.

It was also established that very frequently a prime contractor does not perform any part of the actual work, but subcontracts the whole job out to other pipe line contractors, or the prime contractor sometimes retains a section or sections for his own completion and lets out sections of the pipe line to other contractors.

There was considerable evidence adduced as to the method of arriving at the compensation as between the prime contractor and the subcontractor. Obviously the prime contractor would seek to retain as much of contemplated profit as possible and the subcontractor would endeavour to obtain as much profit as was possible which would be determined by negotiation. The methods of payment vary, the most common methods being on a unit price basis or on a percentage basis and more rarely a lump sum payment.

In the present case the estimated profit of Canadian Pipe Line Co. Ltd. for its share of the work was approximately $500,000. Therefore it follows that the appellant was prepared to expend the amount of $230,000 for the prospect of earning that estimated profit.

In my opinion the method of payment determined upon does not have a material bearing on the essential nature of the transaction.

In *Royal Trust Company v. Minister of National Revenue*[1] the President of this Court categorically stated that in a case under the *Income Tax Act* the first matter to be

[1] [1957] C.T.C. 32.

determined in deciding whether an outlay or expense is outside the prohibition of section 12(1)(*a*) of the Act, is whether it is made or incurred by the taxpayer in accordance with the ordinary principles of commercial trading or well accepted principles of business practice.

In my opinion there is no doubt that it was consistent with accepted business practice in this particular trade for the appellant to make the payment in question.

Having so concluded the next step is to consider whether the deduction of the amount in question is prohibited by section 12(1)(*a*) or falls within its expressed exception. The mere fact that the outlay or expense was made or incurred by the taxpayer in accordance with the principles of commercial trading and was consistent with good business practice does not automatically make it deductible for income tax purposes.

The essential limitation expressed in section 12(1)(*a*) is that the outlay or expense should have been made by the appellant "for the purpose" of gaining or producing income "from the business".

This I think to be the situation in the present case. The appellant is in the business of constructing pipe lines. When control of the appellant company was acquired by its present parent company a vigorous policy was inaugurated. Having been unsuccessful in obtaining the prime contract the appellant set about getting as much of that contract as it possibly could. This was done by acquiring from Canadian Pipe Line Construction Co. Ltd., one party to the joint venture, the rights of that party in the prime contract and in its subcontracts and the appellant eventually entered into a novation back to the owner with the appellant standing in the stead of Canadian Pipe Line Construction Co. Ltd. Had the appellant not done so it would not have been able to do as much of the construction of the pipe line as it thereby did. The income of the appellant is derived from building pipe lines, but in order to earn that income it must first obtain the work. The conduct of the appellant was directed to obtaining participation in the contract work as a means to the end of earning income.

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The next provision relied upon by the respondent is section 12(1)(*b*) of the Act which for the purpose of convenience is repeated here.

> In computing income, no deduction shall be made in respect of,
> (*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part.

The classical statement as to what constitutes a capital outlay is that of Lord Cave in *British Insulated and Helsby Cables Limited v. Atherton*,[1] at page 213.

> But when an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital.

Applying that test to the present case, the payment in question did not bring into existence any advantage for the enduring benefit of the appellant's trade within the meaning of the statement of Lord Cave because "enduring" as used in that context undoubtedly means enduring in the way that fixed capital endures. In the present case the work covered by the agreement was completed within the fiscal year of the appellant and that work was but one job in the business of the appellant from which it earned its income. Therefore, it follows that the true nature of the expenditure was to acquire the means of earning a profit and accordingly the expenditure was laid out as part of the process of profit earning.

Counsel for the respondent submitted that the joint venture agreement between Mannix Ltd. and Canadian Pipe Line Construction Co. Ltd. dated October 1, 1951, was a partnership or syndicate interest and that the agreement between the appellant and Canadian Pipe Line Construction Co. Ltd. outlined in the letter dated April 3, 1952, from Canadian Pipe Line Construction Co. Ltd. to the appellant, was in effect a sale of that interest to the appellant and therefore the payment of $230,000 made to acquire this interest was a capital outlay.

Counsel for the respondent then placed reliance on, *The City of London Contract Corporation, Limited v. Styles*,[2] and *John Smith and Son v. Moore*[3]. However, in neither of

[1] [1926] A.C. 205. [2] (1887) 2 T.C. 239.
[3] [1921] 2 A.C. 13.

these cases were the circumstances similar to those in the present case. In *The City of London Contract Corporation Limited v. Styles* the taxpayer purchased a continuing business as a whole, whatever it consisted of, and accordingly the purchase price so paid was the caapital with which the taxpayer embarked in business, and to carry on that business other moneys must be found. The business acquired was that of carrying on contracts for works and as part of the business the contracts on hand were purchased. The outlay was made to acquire the concern rather than for the purpose of carrying on the concern.

In *John Smith and Son v. Moore* the underlying structure of the business rested upon forward coal contracts which had been negotiated on most advantageous terms. The whole price paid was a sum employed, or intended to be employed, as capital in the trade of the company and was not paid as an outlay in an already acquired business in order to carry it on and to earn a profit out of this expense.

The present case differs in that what the appellant acquired from Canadian Pipe Line Construction Co. Ltd. was the right to perform the work rather than Canadian Pipe Line Construction Co. Ltd. and the right to enter into a novation with Trans-Northern Pipeline which in fact it did by the agreement dated April 30, 1952.

Had the appellant been successful in its attempt to obtain the prime contract there is no doubt that expenses incurred in negotiating that contract would not have been a capital outlay. Accordingly it would follow that expenses incurred to acquire the prime contract or a part thereof from the successful contractor and the right to enter into a novation with the owner would properly be a revenue expenditure rather than a capital outlay.

The Supreme Court of Canada, in *General Construction Company Limited v. The Minister of National Revenue*[1], dealt with this specific problem. In that case counsel for the appellant argued the sale of an interest in a joint venture was the sale of a partnership interest and was therefore

[1] [1959] S.C.R 729.

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the sale of a capital item. Martland J. in delivering the judgment of the Court rejected that argument. The appellant, General Construction Company Limited, made a business of entering into joint ventures with a view to profit. The joint venture was entered into with the intention of investing moneys in the joint venture and of recouping the same, plus a profit, at the conclusion of the venture.

The Canadian Pipe Line Construction Co. Ltd. in the present instance entered into the joint venture with the intention of doing its allocated part of the work at a profit and when the interest was sold to the present appellant it was not the intention of Canadian Pipe Line Construction Co. Ltd. to sell, nor was it the intention of the present appellant to buy an interest in a going concern.

I am satisfied, on full consideration, that the payment of $230,000 made by the appellant herein was an outlay or expense made or incurred for the purpose of gaining or producing income from its business within the meaning of the exception expressed in section 12(1)(*a*) of the Act and not a capital outlay within the meaning of section 12(1)(*b*).

The appeal herein is therefore allowed with costs.

Judgment accordingly.

BETWEEN:

1961
Sept. 28

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

1962
May 30

AND

WILLIAM HEDLEY MacINNES .....RESPONDENT.

Revenue—Income tax—Income War Tax Act, R.S.C. 1927, c. 97, s. 3—Income Tax Act 1948, S. of C. 1948, c. 52, ss. 3, 4, 127(1)(e)—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e)—Profits from mortgages purchased at a discount—Capital gain or income.

The respondent taxpayer who for some years had been engaged in a soap manufacturing operation and in earlier years had had a wide experience in different fields of business activity and in managing estates as official administrator, in 1943 or 1944 was offered at a discount some mortgages and agreements of sale of private homes in Vancouver. He bought a few of these and having found after a time that they were a satisfactory way to invest his money he converted his other investments into cash and invested the proceeds as well as current savings in mortgages and agreements of this kind. Between 1944 and 1954 he purchased a total of 309 mortgages and agreements from those offered to him by various real estate agents without solicitation on his part all at a discount. One hundred and thirteen of these mortgages and agreements of sale were paid off during the years in question and the sums realized from them were treated by the Minister of National Revenue as income in the hands of the respondent and assessed accordingly. The respondent contended that such discounts should be treated as capital increments. An appeal to the Tax Appeal Board was allowed on the ground that the reassessment made for the years 1946 to 1951 were invalid because they were made beyond the time limit prescribed by the statutes and that the discounts received in all the years 1946 to 1954 were accretions of capital. The Minister appealed to this Court and on the hearing of the appeal counsel for the respondent admitted the right of the Minister to make the reassessments when they were made. The securities purchased were not of the kind in which mortgage companies were interested since, though constituting a first charge the principal amount in each case represented up to two-thirds of the value of the property and the companies were unwilling to invest beyond 45 to 50 per cent of the value and also because the mortgage companies were more interested in larger mortgages which met their requirements. The taxpayer was not the lender in any of these transactions and never sold or disposed of any of the mortgages except on very rare occasions for special reasons.

Held: That the discounts realized by the respondent in the years in question were simply enhancements of value on the realization of investments and not gains made in an operation of business in carrying out a scheme for profit making.

2. That the gains realized on the discounts in the years 1946, 1947 and 1948 were not profits from a trade or business within the meaning of the definition of income in s. 3 of the *Income War Tax Act* R.S.C.

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1927, c. 97 nor were the gains realized on discounts in the years 1949-1954 inclusive income within the meaning of the *Income Tax Acts* 1948, S. of C. 1948, c. 52 and R.S.C. 1952, c. 148.

APPEAL under the *Income Tax Act*.

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

Harvey J. Grey and *T. E. Jackson* for appellant.

W. M. Carlyle and *John Fraser* for respondent.

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

THURLOW J. now (May 30, 1962) delivered the following judgment:

This is an appeal from a judgment of the Tax Appeal Board[1] allowing the appeal of the respondent from re-assessments of income tax for the years 1946 to 1954 inclusive. By its judgment the Board held that certain discounts realized by the respondent on mortgages and agreements of sale which had been included in the Minister's computation of the respondent's income for the years in question were not income and it also held that the re-assessments for the years 1946 to 1951 inclusive were invalid and void by reason of their having been made later than the time permitted therefor by the statute. In this court counsel for the respondent admitted the right of the Minister to make the re-assessments when they were made and the only issue raised was that of whether the respondent is liable to tax in respect of the discounts. The amounts of such discounts have been agreed between the parties as follows, these amounts being for each of the years except 1946 and 1949 somewhat less than the amount which the Minister included in his computations of the respondent's income:

1946	$ 750.00
1947	968.23
1948	1,523.17
1949	711.73
1950	1,397.00
1951	5,798.11
1952	8,212.72
1953	8,703.35
1954	10,667.67
	$ 38,731.98

[1] 22 Tax A.B.C. 120.

For the years 1946, 1947 and 1948 the applicable statute was *The Income War Tax Act* R.S.C. 1927, c. 97. by section 3 of which income was defined as meaning "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 including, etc.". The words "trade" and "business" were not defined in the statute and it will be noted that the definition of "income" particularly included the interest received from money at interest "upon any security" or from any other "investment". It is not contended that the discounts in question for the years to which *The Income War Tax Act* applies were "interest" within the meaning of this provision and the liability of the respondent to tax in respect of the discounts realized by him in those years must stand or fall on the issue of whether or not they were profits or gains from any "trade" or "business" within the meaning of s. 3 of the Act.

For the years 1949, 1950, 1951 and 1952 the applicable statute was the *Income Tax Act,* S. of C. 1948, c. 52 and for the years 1953 and 1954 the *Income Tax Act,* R.S.C., 1952, c. 148. The relevant provisions of these statutes were ss. 3 and 4 which were the same in both statutes and s. 127(1)(*e*) of the 1948 Act which was merely renumbered as s. 139(1)(*e*) in the 1952 Act. These provisions were 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,

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(*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)(*e*)—later 139(1)(*e*). 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.

For each of the years 1949 to 1954 the issue turns on whether or not the discounts were income from a business within the meaning of these provisions. This issue is the same as that which arose on the same statutory provisions in a number of cases in this Court having facts somewhat similar to those of the present case including *Cohen v. M.N.R.*[1]; *M.N.R. v. Spencer*[2]; *Scott v. M.N.R.*[3] and *M.N.R. v. Minden*[4]; but while principles for resolving such an issue are discussed in these cases in the end each of them in my opinion is simply a judgment on its particular facts, for as the President of this Court observed in the *Spencer* case at p. 125:

> Indeed there is no rule of general application in cases of the kind referred to except that in every case the question whether the profits realized by a person who has purchased mortgages at a discount or acquired them with a bonus are enhancements of the value of investments or gains made "in an operation of business in a scheme for profit making" or profits from an adventure or adventures in the nature of trade and therefore income within the meaning of ss. 3 and 4 of the *Income Tax Act* is a question of fact and its determination must depend on the facts and surrounding circumstances of the case and the true nature of the transactions from which the profits were realized.

In *Californian Copper Syndicate (Limited and Reduced) v. Harris*[5], the Lord Justice Clerk in a passage which has been referred to and quoted with approval in many subsequent cases explained the distinction between gains that are assessable to income tax and those that are not and posed the test to be applied in determining on which side of the line particular gains may fall as follows at p. 165:

> 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

[1] [1957] Ex. C.R. 236.
[2] [1961] C.T.C. 107.
[3] [1961] C.T.C. 451.
[4] [1962] C.T.C. 79.
[5] (1904) 5 T.C. 159.

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. The simplest case is that of a person or association of persons buying and selling lands or securities speculatively, in order to make gain, dealing in such investments as a business, and thereby seeking to make profits. There are many companies which in their very inception are formed for such a purpose, and in these cases it is not doubtful that, where they make a gain by a realisation, the gain they make is liable to be assessed for Income Tax.

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?

I turn now to the facts as given in evidence by the respondent who was the only witness called at the hearing of the appeal. At that time he was in his 83rd year and he impressed me as being a man of extraordinary intelligence and alertness, who expressed himself in a ready and accurate flow of language. Despite his interest in the result of the proceedings, I think he was perfectly frank and honest in his answers and I neither discount nor doubt any of his testimony.

In the course of his lifetime the respondent has had experience in a number of fields. Following his graduation from high school in 1895, he worked first for a Montreal firm buying hay, then for the Canadian Pacific Railway for several years and later came to Vancouver where he became the manager of a firm dealing in securities and a member of the Vancouver Stock Exchange. In the period between 1900 and the commencement of the Great War he also bought and sold real estate consisting of building lots in Vancouver. During the war he and an associate had an agency for a tire company and operated a retail tire business. From 1918 to 1925 he was Civil Service Commissioner for the Province of British Columbia and later was Official Administrator of the County of Vancouver. He lost his position following a change of government and thereafter joined a firm engaged in the wholesale grocery business. This business, however, did not succeed and in the mid-thirties it was closed. In 1937 he began doing business as a soap manufacturer under the trade name of Western Soap Company and he continued to operate this business as his own until the end of 1954 when he had reached 75. It was then taken

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over by a corporation of which he was the chief shareholder and president. Since then the share control of the company and most of the responsibility for its operations have passed to his son but he remains president and still takes an active part in the business. The respondent began this business after others had failed in it and he managed to make it a successful enterprise by dint of much work on his own part and the reduction of overhead to the barest minimum. He regularly or frequently worked from 9:30 a.m. to 1:30 a.m. the following day, attending personally to the buying and selling and the invoicing, bookkeeping and correspondence as well as the supervising of the manufacturing operation. He employed from 10 to 15 men in the plant including a foreman but had no buyer, salesman, bookkeeper, stenographer or clerk and no office at the plant. The office work was done at his home until the take-over by the company when a small office was built at the plant and a stenographer employed on a part time basis. Having thus eliminated excessive overhead and having concentrated on selling his product to institutions and other users of soap in large quantities who were not attracted by expensive packaging—which he also avoided—he was able to compete successfully with the largest producers of soap and to earn substantial profits but at the cost of prodigious personal effort.

While prior to the incorporation the soap business and its profits belonged entirely to him, for accounting purposes he always treated the business as a separate entity, charging a salary for himself and accumulating in it a reserve against the time when it might be needed for change or expansion of the business. By 1954 the amount which he had accumulated and earmarked as such reserve was approximately $80,000 and this reserve was transferred to the company as part of the assets of the undertaking. At that time the reserve was invested in mortgages and agreements of sale as was the rest of the respondent's savings.

The respondent is a man of simple and frugal personal habits. He neither drinks nor smokes nor gambles, he has lived in the same home since the early thirties and despite his means he drives a 1948 Plymouth car. He has an unusual and favourable arrangement with his banks in respect to exchange charges. He has always managed to live within his income and save something. It is not surprising that such a man would have from time to time moneys which he

would want to put to work and he had not the slightest hesitation in saying so and that he wanted the utmost return from them that he could get without undue risk of loss.

In his early years he liked power stocks and invested money in them and later after coming to Vancouver he also invested in building lots until the beginning of the Great War when the market for them collapsed. He said he both made and lost money in real estate during that period. At the time when he ceased to be Official Administrator of the County of Vancouver there were 2 or 3 estates the administration of which had not been completed and the heirs arranged for him to continue as administrator. Some of these people wanted money earlier than it was available and at their request he purchased assets of the estates consisting of several properties which had been quit claimed by the mortgagor or purchaser and about 10 long term mortgages and agreements of sale. In the case of a number of the mortgages and agreements of sale, the land was ultimately quit claimed to him. He later sold these properties taking agreements of sale or mortgages to secure the unpaid balance of the selling price and the proceeds provided some of the funds with which he later bought other mortgages and agreements of sale but none of the discounts in question arose from transactions in which he sold property which he himself had owned.

These arose in a different way. In the course of his experience as official administrator of the County of Vancouver, he had been surprised to find how well a certain type of what were regarded as substandard mortgages had been paid and that these had a better record than some kinds of mortgages which the mortgage companies regarded as superior. He observed that where a working couple had bought a home at a price that was commensurate with their income, which gave them the accommodation they needed, and had paid a substantial down payment, barring marital trouble, they would pay for it. With this knowledge he was of a mixed mind when in 1943 or 1944 some such mortgages and agreements of sale were offered to him by a friend of his who was in the real estate business. He regarded them as "pretty risky". In his experience buoyant conditions were usually followed by depressions and he did not expect the boom conditions which were generated by the war to last

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as they did. But he was interested in finding investments that would yield more than the 3 or 4 per cent. obtainable on government and other securities and when reminded of his experience he decided to try some of these mortgages. Later when they turned out well he decided to put more money into similar mortgages and agreements. By buying them at a suitable discount these securities though carrying a rate of 6 per cent. would yield 7 per cent. or higher on his investment over their term and the risk of loss on particular mortgages or agreements would be protected and spread by the discounts. Ultimately he disposed of the whole of his other investments and invested the proceeds together with all his current savings and the soap business reserve into mortgages and agreements of sale of this type. From the time of his first purchase in 1943 or 1944 to the end of 1954 he purchased 309 of these securities of which in the meantime 113 had been paid off giving rise to the receipt of the sums in question which have been referred to as discounts.

These mortgages and agreements of sale (which I shall refer to simply as mortgages) were regarded as substandard for two reasons. They all constituted first charges on property, but the principal amount represented up to two-thirds of the value of the property rather than 45 to 50 per cent. which mortgage companies were prepared to advance. To the extent that the amount exceeded 45 to 50 per cent. of the value, the risk was, therefore, similar to that attaching to a second mortgage. The other feature was that they were all small mortgages ranging for the most part between $1,500 and $3,000 and the mortgage companies preferred larger loans which entailed proportionately less bookkeeping and expense. All but 2 of the mortgages which were paid off during the years in question carried an interest rate of 6 per cent. and they were all repayable in monthly payments ranging from $22 to $75 consisting in part of accrued interest and the remainder on account of principal. As the respondent purchased all of these mortgages at a discount the effective return of interest on the amount which he paid was in each case higher than 6 per cent. In 55 cases it was 7 per cent., in 22 cases more than 7 per cent. and in 23 cases between 6 and 7 per cent. In no case did it reach 8 per cent. He also enjoyed the advantage of having his interest paid monthly and, therefore, available for investment earlier than if it

had been payable quarterly or half yearly. Throughout the years in question, economic conditions were buoyant and the mortgages were all paid at maturity or earlier and he continued to invest and reinvest the proceeds in mortgages of this kind. By the time of the trial, however, a number of them had gone into default. He had sustained some losses and could foresee others and had commenced to invest in some other kinds of securities as well.

The evidence indicates that in general the size of the principal amounts of the mortgages acquired by the respondent increased as time went by, the earlier ones being for the most part less than $2,000 and the later ones higher than that amount, the largest being $4,900. The principal of 13 of the mortgages was less than $1,500 and of 21 of them was over $3,000. The discounts at which they were acquired ranged from 6 to 22 per cent. but in 52 of the 113 mortgages which were paid off during the years in question it was exactly 15 per cent. The terms of these mortgages were as follows:

3 years and under 4 years	11
4 years and under 5 years	11
5 years and under 6 years	24
6 years and under 7 years	19
7 years and under 8 years	17
8 years and over	26

One was as short as 2 years and it was the lone case wherein the discount was as low as 6 per cent. The longest term was 13 years. In general the shorter terms were in the mortgages purchased in the earlier years and longer in those acquired in the later years. A rough calculation indicates that in mortgages carrying 6 per cent. interest with a 5 year repayment term a discount of 15 per cent. is only slightly less in amount than the total interest payable over the term. In the case of some of the respondent's purchases the amount of the discount must have been greater than the total interest to be paid over the term while in others it was obviously much less.

The mortgages in question were all selected by the respondent from those offered to him by real estate agents. He never solicited them nor had he any arrangements with the agents to find them for him. During the same period he was offered second mortgages at much higher discounts

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and higher rates of interest, but he turned them down as he also did the numerous offerings of other kinds of securities which arrived in his mail and were committed to his waste basket. He knew precisely the kind of security that he was interested in and was too busy with his soap business to study and consider others. As the number of these mortgages grew, the work of keeping track of the payments increased, and from 1948 to 1952 a real estate agent in whom he had particular confidence, collected the payments for him pursuant to an arrangement under which the agent was to receive 50 cents for each payment collected. Ultimately the agent found this arrangement unprofitable and it was discontinued. Thereafter the respondent attended to the work himself. Most of the payments were received by post and he said that it took him as much as a half hour some days to make the entries, compute the interest, write the receipts and put them in the mail.

The respondent was not the lender in any of these transactions. Without exception what he agreed to do was to purchase from the person entitled thereto the obligation of a borrower together with the security therefor which the holder of the obligation had. In some cases where the transaction occurred as part of the arrangements on the sale of a property, the agent would, in order to save conveyancing costs, arrange to have the mortgage made directly to him rather than to the vendor and then assigned, but this was a mere convenience. The respondent never agreed to lend money to the borrower and in these transactions never dealt with anyone but the agent acting on behalf of the vendor or mortgagee. Throughout the years in question he never sold or disposed of any of the mortgages and has not sold any of them held since then except when it became necessary for him to realize some of them in 1957 or thereabouts to pay income tax assessments and some which he transferred as gifts to charitable institutions. All the rest were not however held to maturity for it frequently happened that a mortgage was paid off ahead of time either on a sale of the property being made or for other reasons. In a very few such instances and for special reasons the respondent acceded to the request of the mortgagee and allowed a small discount but in the great majority of cases the principal and interest were paid in full.

The following summary shows the number and amount of the respondent's purchases of mortgages from 1944 to the end of 1954 together with the discounts recovered.

Year	*Purchases*	*Amount*	*Principal of mortgages purchased*	*No. paid off*	*Discount realized*
1944	3	$ 4,144.50	$ 4,860.00		$
1945	1	914.00	975.00		
1946	23	46,577.66	51,592.02	4	750.00
1947	25	50,169.83	62,529.97	6	968.23
1948	22	49,063.70	60,743.57	8	1,523.17
1949	30	72,096.06	85,423.63	3	711.73
1950	31	78,922.09	96,787.38	5	1,397.00
1951	36	89,790.68	115,802.80	17	5,798.11
1952	60	170,068.41	212,590.07	23	8,212.72
1953	34	115,835.07	148,365.76	18	8,703.35
1954	44	148,394.86	212,714.51	29	10,667.67
	309	$ 825,976.86	$ 1,052,384.71	113	$ 38,731.98

At the end of 1954 he had on hand 196 mortgages with unrealized discounts amounting to $187,675.87 most if not all of which has since been realized and he has also continued to buy additional mortgages at a discount.

I have no hesitation in reaching the conclusion that the discounts totalling $750.00 realized by the respondent in 1946 were not profits from a trade or business within the meaning of s. 3 of the *Income War Tax Act*. As I see it these discounts resulted simply from the trial investments in mortgages which the respondent had made in earlier years and I do not think it would have occurred to anyone to think at that time that in buying and holding them to maturity he was engaged in a trade or business rather than merely investing his money and holding the investments. Nor can what he did in 1946 and later in buying more mortgages of the same type change the nature of what he had done earlier for even if his subsequent purchases and conduct were considered to amount to a business within the meaning of the statute that, in my opinion, would at most be evidence from which an inference might be drawn that the earlier transactions were also transactions in the course of the same trade or business, an inference which in my view should not be drawn in view of the respondent's evidence as to how he came to make his first purchases of

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the mortgages. For 1946 I am accordingly of the opinion that the judgment appealed from insofar as it holds the discounts not subject to tax is correct and should be affirmed.

With respect to the sums of $968.23 and $1,523.17 in discounts realized in 1947 and 1948 the result is perhaps not quite so plain but I have little difficulty in reaching the conclusion that these sums as well were not income from a trade or business within the meaning of s. 3 of the *Income War Tax Act*. Granting that in 1946 the respondent had begun changing his other investments into mortgages of this kind and had bought 23 mortgages at a cost of $46,577.66, and in 1947 a further 25 mortgages at a cost of $50,169.83 from the payment of which the sums of $968.23 and $1,523.17 were probably for the most part realized and also taking into account that in 1948 as well he had bought another 22 mortgages at a cost of $49,063.70 and that he continued to buy mortgages on a substantial scale in later years, I am unable to see what there was about the respondent's purchases, holding and receiving of the amounts accruing on these mortgages to characterize what he did as a trade or business rather than as a mere investing of his funds in mortgages and the holding of such investments. The case for characterizing what he did as a trade or business appears to me to be weaker than that in *Argue v. M.N.R.*[1] where the taxpayer besides acting as manager of a loan company which brought him in close contact with mortgage transactions and gave him a special knowledge of that field invested his own money in mortgages and agreements of sale of an average principal of $1,300—to a total extent of $102,379.24, also loaned some money on the security of promissory notes and combined with these activities that of a fire insurance agent—a business capable of being carried on as an incident or side line of a business in mortgages yet the Supreme Court held that the taxpayer's income from the mortgages was not profit from "carrying on one or more businesses, as defined in s. 3 of the *Income War Tax Act*" within the meaning of s. 2 (1)(*g*) of the *Excess Profits Tax Act*, 1940; S. of C. 1940, c. 32.

[1] [1948] S.C.R. 469.

The Minister's case with respect to the discounts realized in 1947 and 1948 accordingly fails as well though as will appear what I shall have to say with respect to the discounts realized in the years 1949-1954 applies with equal effect with respect to 1947 and 1948 for while the definition in s. 127 (1)(*e*) of the *Income Tax Act* expanded the ordinary meaning of the word "business" so as to include "an adventure or concern in the nature of trade", it appears to me that this has little effect in this particular case because in view of the number of transactions involved it would seem to me that if the case is not one falling within the ordinary meaning of the word "trade" it is outside the scope of the expression "adventure or concern in the nature of trade" as well.

After lengthy consideration of the facts I am of the opinion that the discounts realized in the years 1949 to 1954 were not profits from a business within the meaning of that term as defined in the applicable statutes. In my view there is nothing in the case which characterizes what the respondent did as anything but mere investment of funds which he had available for investment. What the respondent did in the years in question was simply to buy mortgages, hold them to maturity and receive the payments when made. He undoubtedly had a more than ordinary ability to appraise the several factors entering into a judgment of when to buy and when to refuse what was offered and he knew how to select with a minimum of effort the mortgages he would buy. But any investor who proposes to obtain a revenue from his means while at the same time protecting his capital must have some knowledge of what he is about or he is not likely to be an investor for long. Nor was there in my view anything about the way in which he acquired them which is not as consistent with mere investment of funds as with the carrying on of a business. Moreover, he did not buy the mortgages to sell and did not sell them. No doubt he held them to get from them all that he could including the discounts but it would I think be unrealistic to look upon what he did as a course of conduct or scheme directed primarily to the making of profit by realizing such discounts. The interest return was of greater importance and the most that could be said on this score is that his object was to get both.

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But that is the same object which anyone has who buys a bond at a discount intending to hold it to maturity. And in any case the matter is not governed by the intention to make a gain or profit. Intention to make a profit in a particular way is no doubt an important fact to be considered in cases of this kind but like many of the other features which are from time to time referred to in such cases as pointing to one conclusion or another its importance depends on the context of the particular case. In the present case I do not regard it as having much significance. Nor does the fact that he kept records of the mortgages and wrote receipts for the payments and that this in later years took some of his time each day in my opinion make any difference.

Secondly, investment in first mortgages of real estate is a well known and recognized way of investing money to obtain an income return. Here the mortgages were substandard—in the sense that mortgage companies were not interested in them—but the matter is not dependent on the standards of mortgage companies which may be as high or low as they see fit to adopt within such restrictions as the law imposes upon them. That these mortgages as a class were in fact good securities is demonstrated by the result and though each involved some risk and at that possibly a somewhat greater risk than the types in which the mortgage companies were interested, I see nothing so unusual about them as to suggest that the respondent chose them in the course of a gamble or adventure looking to the realization of a speculative profit. In no case was he subjecting the whole amount invested to risk of the sort assumed by a second mortgagee who may lose his whole investment if the value of the property declines below the amount of the prior incumbrance. Moreover when buying at a discount of 15 per cent. a mortgage with a principal amount equal to two-thirds of the value of the property he was investing in it only to the extent of 56⅔ per cent. of the value of the property and under the repayment terms that would be reduced as each month went by. What he paid for these mortgages was no doubt as much as anyone would pay and represented what they were worth to any prudent investor seeking a high income return who knew their characteristics and took into account such risk as attached to them. Moreover except in a few cases, they

were not short term mortgages nor is there any occasion to infer that they were acquired in the expectation that they would be paid before maturity.

To my mind the only features about this case which tend to suggest that what the respondent did amounted to a business are the multiplicity of the transactions and the systematic course of conduct which the respondent pursued in investing and reinvesting in these mortgages. As I see it nothing about the acquiring, holding or realization of any one of the mortgages indicates a business and it is only if the number of transactions and the system pursued make a difference—when viewed with the other facts—that there is any basis for the suggestion that this was a business within the meaning of the definition. On this question I have a good deal of doubt because of the large total number of transactions but it appears to me that in a case of this kind, that is to say a case of purchases of mortgages by a person whose principal activity is not dealing in mortgages or other securities but soap manufacturing, the number of transactions is so largely a matter of how much money the particular individual has available to invest that I am unable to attribute much weight or effect to it, and the same applies with respect to the system for given the fact of a desire to invest his system indicates nothing but a repetition of the event as often as is necessary to accomplish the object of keeping his money invested and no more. To my mind in the circumstances of this case, these features do not indicate that the respondent was engaged in a commercial enterprise or trade. Over the six-year period 1949-1954 the purchases averaged 3.4 transactions per month. In 1949 the average was 2.5 per month. In 1952 the average was 5 per month, and in 1954 3.6 per month. A person who in transactions similarly numerous and whenever he happened to have money available bought government and corporation bonds at a discount from several dealers intending to hold them to maturity would not in my opinion be regarded as engaged in a trade or business merely because of the number of purchases involved or the fact that he pursued a policy of buying as often as he had money available to do so but only at a discount. The conclusion can I think also be tested by putting a converse case. Suppose the purchaser of bonds

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in the case suggested or the respondent in buying mortgages instead of buying at a discount in each case paid a premium. In neither case can I conceive of his being regarded as engaged in a business so as to enable him to deduct the premiums from interest for the purpose of computing his profit.

The Minister's submission with respect to the years 1949 to 1954 accordingly fails as well. In the result I am of the opinion that the discounts realized by the respondent in these years as well as in the earlier years were mere enhancements of value on the realization of investments and not gains made in an operation of business in carrying out a scheme for profit making.

The judgment appealed from will be varied by setting aside the Board's declaration that the re-assessments for the years 1946-1951 inclusive were void *ab initio* and restoring the re-assessments but subject to variation in accordance with these reasons by omitting from the computation of income the discounts realized by the respondent in those years. Subject to this the judgment of the Tax Appeal Board with respect to all the years under appeal will be affirmed and this appeal will be dismissed with costs.

Judgment accordingly.

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Oct. 13, 14

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Mar. 23

BETWEEN:

ALEX MILLER .....APPELLANT;

AND

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

Revenue—Income tax—Income Tax Act, 1948, S. of C. 1948, c. 52, ss. 3, 5, and 16—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 15 and 16(1)—Income or capital receipts—Commissions payable under agreement—Payment on termination of contract—Payments for assignment of rights to commissions—Payments commuting rights to commissions—Commissions in lump sum—Taxation of commissions not received—Whether payments taxable—Appeal allowed—Cross-appeal dismissed.

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Appellant introduced M to a United States manufacturer of parking meters and as a result M obtained an exclusive license under a patent to manufacture and sell these parking meters in Canada. In August 1950, pursuant to the provisions of an earlier agreement between them, the appellant became exclusive sales agent for M in the Province of Quebec and part of Ontario on a commission basis and became entitled on the termination of the agency to a commission of 2½ per cent on sales made in the same territory payable during the life of the appellant so long as the patent existed. In July 1951 M purported to terminate the agency by a notice given pursuant to the agreement and a dispute having arisen as to the validity of such termination, the appellant and M in October 1951 entered into another agreement by which the termination of the agency was confirmed but it was further provided that the appellant should receive $3,750 in instalments and a commission in respect of certain pending sales and his right to the commission of 2½ per cent during his life for the term of the patent was confirmed. Of the $3,750, $1,750 was paid to the appellant in 1952, one of the taxation years with which the appeal is concerned. In the same year the appellant assigned his rights to payment of the commission on the pending sales to A.M.I. in consideration of an immediate payment of $12,000 and 42 per cent of the commissions in excess of that sum. Under this assignment appellant received in 1952 payments of $12,000 and $1,470 and in 1953 received $896.27. In 1953 appellant by a further agreement released his rights to future payments of the 2½ per cent commission in return for an immediate payment of $5,000. The Minister assessed all amounts paid to the appellant under these agreements as subject to tax and on the assumption that s. 16(1) of the *Income Tax Act* applied to the appellant's transaction with A.M.I. also assessed as income of the appellant amounts representing the 58 per cent of the commissions in excess of $12,000 retained by A.M.I. Appellant's appeal to the Tax Appeal Board succeeded with respect to the inclusion in his income of the amounts retained by A.M.I. but in other respects failed. He thereupon appealed to this Court and the Minister cross-appealed seeking to have the assessments restored.

Held: That the $1,750 received in 1952 under the 1951 agreement was not a profit from appellant's business but a capital receipt, and was not subject to tax as income.

2. That the sums of $12,000 and $1,470 received from A.M.I. in 1952 and $896.27 in 1953 were income receipts and subject to tax.

3. That the right of the appellant to the 2½ per cent commission was a right of a capital nature and the $5,000 received by appellant for the release of such right was also capital.

4. That s. 16(1) of the *Income Tax Act* did not apply to the appellant's transaction with A.M.I. and that the cross-appeal failed.

APPEAL under the *Income Tax Act*.

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

G. R. Dryden for appellant.

E. A. Goodman, Q.C. and *J. D. C. Boland* for respondent.

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

THURLOW J. now (March 23, 1962) delivered the following judgment:

This is an appeal from a judgment of the Tax Appeal Board by which appeals by the appellant from re-assessments of income tax for the years 1952 and 1953 were allowed in part. There is also a cross-appeal by which the Minister seeks to have the re-assessments restored. The issue in the appeal is whether certain sums received by the appellant and which are referred to in the outline of the facts which follows, were properly included by the Minister in computing the appellant's income for income tax purposes. The applicable statute for 1952 was the *Income Tax Act*, Statutes of Canada 1948, c. 52, and for 1953 was the *Income Tax Act*, R.S.C. 1952, c. 148, but there is no difference in the applicable provisions. The issue raised by the cross-appeal is whether in the circumstances sums not received by the appellant but by A. M. I. Distributing Co. Ltd. are taxable as income of the appellant under s. 16 of the applicable statute.

The appellant, who at one time had been engaged in manufacturing clothing and later was a part-time employee of a clothing firm, in or about 1938 became interested in parking meters and commenced acquiring information about them. Some years later, while still a part-time employee of the clothing firm, he began operating a parking lot. In 1949 or 1950, he contacted McGee-Hale Park-O-Meter Company, a United States firm which held the Canadian patent on a type of parking meter, and succeeded in getting that firm interested in granting a licence under the patent to manufacture and sell the meters in Canada. He then contacted some fifty or more persons in an endeavour to interest someone with the necessary means in joining in an undertaking for that purpose and ultimately, in August, 1950, concluded a contract with one David A. McCowan by which the latter, with the appellant's consent, which was necessary in view of an earlier contract between them, undertook to negotiate for the patent licence and, upon obtaining it, to appoint the appellant as exclusive sales representative for the Province of Quebec and the portion of Ontario lying east of Fort William and Port Arthur. By the contract, McCowan retained the right to set and change prices and

to control the form of sales contracts and the credit arrangements under which the meters would be sold, and it was also provided that he should not be liable to the appellant for failure to perform a contract with a purchaser by reason of labour trouble or any other cause not within his control, but he reserved no express right to refuse orders secured by the appellant. The appellant, on his part, among other things, undertook to sell a minimum of 375 meters by June 30, 1951, and a minimum of 750 meters each year thereafter, and there were provisions for termination of the agreement if he failed to meet this undertaking. His remuneration was to be a commission at specified rates on the price of meters sold by him or his salesmen, and it was also provided in para. 12 that

> Miller shall not be entitled to commissions on Park-O-Meters which have not been contracted for in writing by a purchaser prior to the termination of this contract or any extention thereof. Provided that in any case where Miller has commenced negotiations for the sale of Park-O-Meters which are not concluded by the date of such termination, Miller shall be allowed 30 days from such date to conclude such sale, and upon obtaining a firm order in writing within such 30 day period, will be entitled to commission thereon as hereinbefore provided.

By a further term of the agreement, the appellant agreed to provide a sales office in Toronto and McCowan undertook to contribute $500 per year towards the cost of such office. By para. 8 it was also provided that if the appellant should become unable to carry out his undertaking or if the agreement were terminated prior to the expiration of the licence under the patent, he should have no further obligation under the contract but would "in consideration of the introduction by him to McGee-Hale and the information and assistance freely given and to be freely given by Miller to McCowan," be entitled to a commission of 2½ per cent. of the selling price of meters thereafter sold by McCowan in the territory so assigned to Miller, for so long as Miller should live and the licence remain in force provided always that Miller should not in the meantime become interested in the manufacture or sale of any other parking meter.

McCowan assigned the contract to Park-O-Meter Co. of Canada, Ltd., a company which he had had incorporated, obtained the patent licence and began manufacture of the meters, but ran into difficulties in obtaining steel and was also hampered by a patent infringement proceeding brought

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when he sold a number of meters to the City of Vancouver. In the meantime, the appellant gave up his part-time employment with the clothing firm and set up a small sales office in Toronto. He had no employees engaged at this office and after some months it was discontinued. Thereafter, he conducted his operations from his home. In this operation, he contacted a number of municipal authorities in Ontario and Quebec, and he spent time and effort in connection with a prospective sale to the City of Toronto of some 1,300 meters. In this connection, a tender by Park-O-Meter Co. of Canada, Ltd. was submitted on June 11, 1951, but it had not been accepted when on July 13, 1951, the appellant was formally notified by McCowan of the termination of his agency in 30 days because of his failure to sell 375 meters by June 30, 1951.

The matter did not, however, rest there. The appellant contacted McCowan, blamed his own failure to sell 375 meters on McCowan's difficulties and the latter's inability or unwillingness to permit him to promise definite delivery dates or to quote firm prices, and asked for a further opportunity to make the sales provided for in the agreement. McCowan declined to accede to this request but offered the appellant a different territory in which to operate and the appellant being dissatisfied with this proposal later put the matter in his solicitor's hands and threatened suit. In the period of 30 days which followed the 30 day period mentioned in the notice of termination, Miller secured an order for meters from the City of Kitchener and a further order from the City of Hamilton.

Ultimately, by an agreement dated October 1, 1951, a settlement was concluded. This agreement, after referring to the earlier agreement, recited that Miller had sold no meters except as thereinfter mentioned, that McCowan on July 13, 1951, had given Miller 30 days' notice of cancellation of the agreement and that Miller disputed the validity of the notice. By this agreement, the termination of the earlier agreement as of August 13, 1951, was confirmed, but McCowan and Park-O-Meter Company of Canada agreed to pay Miller $3,750 in certain instalments extending over a period of six months, $200 for costs, commission at the rate of $13.63 per meter for each meter that should be sold

to the City of Toronto pursuant to the tender already mentioned, and commission as provided in the earlier agreement in respect of the sales to the City of Kitchener and the City of Hamilton of meters for which the appellant had obtained orders prior to September 13, 1951. It was also provided that Miller should have the right to continue to represent McCowan and his company in the negotiations connected with the tender made to the City of Toronto and that McCowan and Park-O-Meter would co-operate and render him every reasonable assistance. Miller was also given a similar right in connection with the order which he had obtained from the City of Kitchener. At the time of the making of this agreement, the tender made to the City of Toronto had been approved by the City Engineer, the City Treasurer and the Police Department, but it was not approved by the Board of Control until October 15, 1951. The provision of the earlier agreement whereby Miller would be entitled on termination of his agency to $2\frac{1}{2}$ per cent. commission on sales made thereafter in his territory remained in force with an alteration in respect of the sales which might be concluded to the Cities of Toronto, Hamilton and Kitchener after August 13, 1951, on which commission was to be paid as provided in the agreement of settlement, and with a further alteration extending Miller's right to such commissions on sales made in the defined territory so long as McCowan or Park-O-Meter of Canada Ltd. or any subsidiary thereof, or any person or company in which McCowan or Park-O-Meter of Canada might be interested either directly or indirectly, should have the right to manufacture or distribute meters in the defined territory during the life of the patent.

Of the $3,750, payments totalling $2,000 were received by the appellant in 1951 and were later reported by him as income for that year. The remaining $1,750 was received in 1952, and it is the first of the amounts in issue which the Minister has assessed and which the appellant contends were not income but capital.

Shortly after the conclusion of this agreement and before he had engaged in any further enterprise or employment, the appellant suffered a heart attack and was an invalid for several months thereafter. During this period, the City of Toronto accepted the tender and on November 21, 1951, entered into a formal contract with Park-O-Meter of Canada

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Ltd. for the purchase and installation of some 1,300 meters, but by the terms of the contract the City had the right after a six-months' trial period to return the meters at any time during a further period of six months. Early in February 1952, the appellant, being in need of money, assigned to A. M. I. Distributing Co. Ltd. all moneys and commissions that might be or become payable to him under the agreement of settlement with McCowan and Park-O-Meter Co. of Canada, Ltd. on the sale of the meters to the City of Toronto and in the assignment he warranted that the commissions payable to him were at the rate of $13.63 on each meter and that the number of meters so sold was not less than 1,339. The consideration for this assignment was $12,000 to be paid at once and 42 per cent. of the moneys received pursuant to it by A. M. I. Distributing Co. Ltd. in excess of $12,000. The remaining 58 per cent. was to be retained by A. M. I. Distributing Co. Ltd.

The $12,000 so received by the appellant in 1952 and the moneys he received in 1952 and 1953 representing 42 per cent. of the surplus have been included in his income by the Minister in making the assessments and together make a second group of amounts in respect of which the liability of the appellant to tax is in issue in the appeal. For the 1952 taxation year, the amount included by the Minister was the $12,000 and $1,500. It is now conceded by the Minister that the amount actually received by the appellant in 1952 representing the 42 per cent. was $1,470—an amount which the appellant had reported as income in his return. It is not, however, conceded that the appellant is entitled to relief in respect of the tax on the difference of $30. In re-assessing the tax following the appellant's notice of objections, the Minister had (erroneously) assumed that the $1,500 represented the whole amount paid by Park-O-Meter of Canada, Ltd. to A. M. I. Distributing Co. Ltd. and had assessed the appellant on the assumption that he was liable to tax on the whole of such amount. In the Tax Appeal Board the appellant succeeded in respect of the taxation in his hands of amounts representing A. M. I.'s 58 per cent. of the amounts received from Park-O-Meter of Canada Ltd. but by his cross-appeal the Minister seeks to have the assessment in respect of this amount restored. This item of $30 is thus in issue on the Minister's cross-appeal for 1952.

For the 1953 taxation year, the amount included by the Minister as representing the commissions paid by Park-O-Meter of Canada Ltd. was $2,110.16, but it is now conceded by the Minister that this amount should be reduced to $896.27, which represents only the 42 per cent. received by the appellant in the year and which was reported by him as income in his income tax return. The appellant is accordingly entitled to relief from the tax imposed in respect of $1,213.89 of the income as assessed and his appeal for 1953 succeeds to that extent. The amount of $896.27 is, however, still in issue, the appellant contending that it was not income for the purposes of the *Income Tax Act*. As a result of the concession mentioned, no issue remains on the cross-appeal in respect of the year 1953.

Some time after his recovery from his illness, the appellant began selling coin vending machines under an arrangement with another firm and in 1953 decided to buy some of the machines to operate on his own. Requiring money for this purpose, he contacted McCowan and offered to release all his rights to payments accruing in the future under the agreements already mentioned for $5,000. The offer was accepted, the appellant received $5,650, made up of the $5,000 and $650 for amounts already accrued and payable, and he executed a release dated October 14, 1953 of his right to 2½ per cent. in respect of sales made in his former territory and further covenanted not to engage or be concerned in manufacturing or disposing of parking meters in Canada for seven and a half years. The $5,650 so received was included by the Minister in his computation of the appellant's income for 1953. The appellant did not dispute his liability to tax on the $650 but issue arises in respect of the $5,000 which the appellant contends was not income but capital.

To recapitulate, the amounts received by the appellant on which issue arises in the appeal and cross-appeal are:

For 1952

(1) $1,750.00 received by appellant in 1952 from Park-O-Meter of Canada Ltd. as part of the $3,750 payable under the settlement agreement of October 1, 1951.

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(2) $12,000.00 received by appellant in 1952 from A. M. I. Distributing Co. Ltd. being part of the consideration for the assignment made in 1952 of amounts payable by Park-O-Meter of Canada Ltd. under the settlement agreement of October 1, 1951.

(3) $1,470.00 received by the appellant in 1952 from A. M. I. Distributing Co. Ltd. representing the 42% payable to him under the assignment referred to in (2) above.

(4) $30 not received by the appellant but representing part of the 58% to be retained by A. M. I. Distributing Co. Ltd. under the assignment referred to in (2) above.

For 1953

(5) $896.27 received by appellant in 1953 from A. M. I. Distributing Co. Ltd. representing the 42% payable to him under the assignment referred to in (2) above.

(6) $5,000.00 received by appellant in 1953 from Park-O-Meter of Canada Ltd. pursuant to the release of October 14, 1953.

The case put forward on behalf of the appellant consisted of three main submissions. First, it was said that the settlement agreement of October 1, 1951, was in fact a settlement of a claim for damages for breach of the agency agreement, that the sums payable to the appellant pursuant to the settlement agreement were in substance and in fact damages for loss of the agency contract and that therefore they were capital and not income.

Secondly, it was contended that even if the sums payable under the settlement agreement and referred to therein as commissions were of an income nature the right to them was contingent on the contract between Park-O-Meter of Canada Ltd. and the City of Toronto being consummated by ultimate purchase of the meters, and that because the appellant's right to such sums at the time he assigned it to A. M. I. Distributing Co. Ltd. was contingent the amount paid by A. M. I. to him for the assignment must be regarded as capital and not as income.

Finally, it was submitted that the $5,000 received by the appellant from Park-O-Meter of Canada Ltd. pursuant to the agreement of October 14, 1953, was received in exchange

for his right to 2½ per cent. on sales made in his former territory, under the agreement of August 1950, which was a capital asset and that the sum so received was therefore capital as well and not taxable as income. In advancing these submissions, Mr. Dryden treated it as immaterial whether the relationship between McCowan and the appellant evidenced by the agreement of August 29, 1950, was one of employer and employee or one of principal and agent wherein the agent was engaged in carrying on a business of his own.

Mr. Goodman on behalf of the Minister took the position that the appellant was not an employee but was carrying on a business of his own. Indeed, in the Minister's amended reply, it is pleaded as the basis of the taxation that the appellant in 1952 and 1953 was in the business of selling parking meters to the City of Toronto and elsewhere in Ontario and that the profit from the business in 1952 and 1953 was not less than $13,500 and $2,110.16, respectively. It is also pleaded as the basis for taxation of the $5,650 that it was received for the cancellation of an agency agreement entered into by the appellant in the course of his business and was therefore income by virtue of the provisions of s. 3 and s. 5 of the *Income Tax Act*.

Mr. Goodman's submission with respect to the $1,750 paid under the agreement of settlement of October 1, 1951, was that while the agreement does not show how the payment was calculated or what it represented, in the circumstances, it would be proper to regard it as a *quantum meruit* for services which had been rendered up to the time of termination of the agency, and that it would accordingly be income. With respect to the $1,200 and the 42 per cent. of the sum over that amount paid by Park-O-Meter, his submission was that the $13.63 per meter sold to the City of Toronto was commission in fact as well as in name and represented profit from the carrying on of the agency, that in fact what the agreement of settlement did was not to completely terminate the agency but to preserve it in respect of the negotiations with the City of Toronto with alterations in the commission arrangement, and that such amounts accrued from the carrying on of the agency relationship under such altered arrangements and were accordingly income; and further that the assignment of the appellant's rights to such sums to A. M. I. Distributing Co. Ltd. has no effect on their

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character as income. He also submitted that the whole sum representing the $13.63 per meter was income of the appellant and taxable in his hands under s. 16(1) of the *Income Tax Act* since the assignment to A. M. I. Distributing Company amounted to the conferring of a benefit on the assignee within the meaning of that subsection. He conceded, however, that if s. 16(1) was inapplicable, the cross-appeal must fail. Finally, he submitted that the right to 2½ per cent. on sales of parking meters in Eastern Ontario and Quebec which the appellant was to receive for his life or so long as the patent licence was held by Park-O-Meter of Canada Ltd. was granted for services which he had rendered and was to render and was therefore of an income nature and that the amount of $5,000 which he received in consideration for the release of such right was income as well.

In my opinion, the evidence clearly establishes that the appellant was never an officer or employee in the service of McCowan or of Park-O-Meter. As I view it, from the time of the establishment of the relationship, the appellant simply had an agency contract with McCowan and Park-O-Meter of Canada Ltd. and was independent of and not subject to regulation by McCowan or that company in carrying out his activities within the limits which the contract prescribed. The sums in question are accordingly not taxable as income from an office or employment and if income at all are taxable as income from his business.

I turn now to the sums which became payable under the settlement agreement of October 1, 1951. The question of when sums payable in connection with the termination of business arrangements are to be regarded as profits of a business and when as capital receipts has been considered in a number of English and Scottish cases which were referred to in the course of the argument and the principles applied in them appear from the following extracts. In *Commissioners of Inland Revenue v. Fleming & Co. (Machinery), Ltd.*[1], Lord Russell stated the matter thus, at p. 63:

> The sum received by a commercial firm as compensation for the loss sustained by the cancellation of a trading contract or the premature termination of an agency agreement may in the recipient's hands be regarded either as a capital receipt or as a trading receipt forming part of the trading profit. It may be difficult to formulate a general principle by reference to which in all cases the correct decision will be arrived at since in each case the question comes to be one of circumstance and

[1] 33 T.C. 57.

degree. When the rights and advantages surrendered on cancellation are such as to destroy or materially to cripple the whole structure of the recipient's profit-making apparatus, involving the serious dislocation of the normal commercial organisation and resulting perhaps in the cutting down of the staff previously required, the recipient of the compensation may properly affirm that the compensation represents the price paid for the loss or sterilisation of a capital asset and is therefore a capital and not a revenue receipt. Illustrations of such cases are to be found in *Van den Berghs, Ltd.* [1935] A.C. 431, and *Barr, Crombie & Co., Ltd.* [1945] S.C. 271. On the other hand when the benefit surrendered on cancellation does not represent the loss of an enduring asset in circumstances such as those above mentioned—where for example the structure of the recipient's business is so fashioned as to absorb the shock as one of the normal incidents to be looked for and where it appears that the compensation received is no more than a surrogatum for the future profits surrendered—the compensation received is in use to be treated as a revenue receipt and not a capital receipt. See e.g., *Short Brothers, Ltd.*, 12 T.C. 955: *Kelsall Parsons & Co.* [1938] S.C. 238.

In *Anglo-French Exploration Co., Ltd. v. Clayson*[1], Lord Evershed, M.R., said at p. 766:

If the matter were res integra, I think there is much to be said for the simple view that a sum of money received in consideration for the giving up or destruction of an agreement under which one looks to earn an annual sum is capital and not income; for in such case the sum received might be fairly described as the capitalised equivalent at the present time of income prospects. The question remains, however, not whether that sum in some senses or in some contexts might sensibly be called a capital payment, but whether it is a profit or gain arising from the trade of the recipient within the terms of Sch. D.

The matter is not in any case res integra. The line of cases starting from the well known trilogy in 12 Tax Cas., of *Inland Revenue Comrs. v. Newcastle Breweries, Ltd.* (at p. 927), *Short Bros., Ltd. v. Inland Revenue Comrs.* (at p. 955) and *Inland Revenue Comrs. v. Northfleet Coal & Ballast Co. Ltd.* (at p. 1102), in 1927, seem to me to emphasise that sums received for the cancellation of an agency or of other similar agreement which has been entered into by the recipient in the ordinary course of its trade will themselves, prima facie, be regarded as received in the ordinary course of trade *unless* the transaction involves a parting by the recipient with a substantial part of its business undertaking. *Barr, Crombie & Co. v. Inland Revenue* (26 Tax Cas. 406), was a case of that exceptional character.

In *Wiseburgh v. Domville*[2], where the payment in question was one of an agreed amount of damages, Lord Evershed, M.R., said at p. 758:

In *Kelsall Parsons & Co. v. Inland Revenue* (21 Tax Cas. 608), Lord Normand (Lord President), said (ibid., at p. 619):

> . . . no infallible criterion emerges from a consideration of the case law. Each case depends upon its own facts . . .

That case is perhaps very much at one end of the line and *Barr,*

[1] [1956] 1 All E.R. 762. [2] [1956] 1 All E.R. 754.

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Crombie & Co. v. Inland Revenue (26 Tax Cas. 406), very much at the other. In the former the business of the taxpayer company was that of agents for manufacturers. At the relevant date they had far more agency contracts than the taxpayer here, however, and the sum under consideration by the Inner House was paid for cancellation of a contract which would have determined in any event in a relatively short time and in regard to which, as Lord Normand says, the taxpayer had no reasonable expectation of its further continuance.

However, junior counsel for the taxpayer points out that the present case is really distinguishable in a significant degree on its facts. First, the taxpayer here held but two agencies. Secondly, although the present agency was expressed to be determinable at relatively short notice, there would have been no reason to suppose that it would have been if all had gone well. And thirdly, as the commissioners pointed out, the effect of the loss of this contract, quoad the taxpayer's agency business was very substantially to depreciate his earnings: whereas in *Kelsall Parsons & Co. v. Inland Revenue* (21 Tax Cas. 608), the court pointed out that the taxpayer's earnings out of the agency business were not much different from what they had been before the cancellation of the material contract. I agree that this case differs in these respects from *Kelsall Parsons & Co. v. Inland Revenue*. But I am unable to agree that those differences are of such significance as to bring it from the territory, so to speak, of *Kelsall Parsons & Co. v. Inland Revenue* into that of *Barr, Crombie & Co. v. Inland Revenue* (26 Tax Cas. 406). On its facts, the present case more closely resembles *Inland Revenue v. Fleming & Co. (Machinery), Ltd.* (33 Tax Cas. 57), and, as already indicated, I must resist counsel's invitation to refuse to follow the Scottish line of authority.

To bring the case within the *Barr, Crombie* territory the taxpayer must be shown to have parted in truth and in substance, not merely with his rights and expectations under a contract entered into in the ordinary course of his trade, but with one of his enduring capital assets, as it is called. On that sort of consideration this case might well have been different if the £4,000 had been paid because the taxpayer's goodwill had been damaged. In *Barr, Crombie & Co. v. Inland Revenue* the agency cancelled amounted to the substance of the whole business of the taxpaying company. Its receipts accounted for nearly nine-tenths of the total earnings and its loss necessitated the complete reorganisation of the company's business, a reduction in their staff, and the taking of new and smaller premises. In effect, a substantial part of the business undertaking had gone.

In the present case there are a number of facts which appear to me to point to the conclusion that the $3,750 which the appellant received under the agreement of settlement should not be regarded as income from the appellant's business. First, it is apparent that the agency contract between the appellant and McCowan or Park-O-Meter Co. of Canada was not one of a number of agency contracts but was the only one which the appellant had. Not only that but the contract was fundamental to the appellant's operation for there was no operation except what was to be done pursuant to the contract. Nor can the contract be properly characterized as one entered into in the ordinary course of

trade or as an incident of the carrying on of the appellant's business. On the contrary, the making of it appears to have been a preliminary step prior to engaging in a trade. And when that contract finally ceased the appellant's operation was at an end. Nor did he afterwards engage in any business in any way connected with or related to the manufacture or distribution of parking meters. Secondly, it was a long term contract which might have continued for the duration of the patent licence and which was not subject to cancellation except for reasons and on terms particularly defined. The contract thus appears to fall, initially, at any rate, in what Lord Evershed, M.R., referred to as "the Barr, Crombie territory". Next, while the agreement of settlement does not state what the $3,750 was being paid for, it does appear that there were no arrears of commissions due to the appellant nor was there anything due or recoverable by him on a *quantum meruit* basis for any services which he had rendered in endeavouring to promote the sale of meters. The only sales in prospect at the time appear to have been those to the Cities of Kitchener, Hamilton and Toronto, and these were elsewhere particularly dealt with in the agreement of settlement. From these facts I would conclude that the $3,750 to which the appellant became entitled under the agreement of settlement was not a settlement or surrogatum for commissions which he might have expected to reap from the activities which he had carried out but was referable to the loss of the contract itself which was not one of a number of similar contracts entered into in the course of his business but was the "fixed framework" within which he operated. Having regard to these features of the situation, I am of the opinion that the $3,750 so received was not a profit from the appellant's business but a capital receipt. The appeal accordingly succeeds in so far as the $1,750 included in the appellant's income for the year 1952 is concerned and the assessment for that year must be varied accordingly.

It is otherwise, however, with respect to the $13.73 per meter provided for by the agreement of settlement with respect to meters which might be sold to the City of Toronto pursuant to the tender. The agency contract itself contemplated the possibility of sales being made within 30 days after termination of the agency as a result of negotiations initiated prior to its termination and I think there could be no doubt that commissions earned on such sales would

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have been income. What the agreement of settlement appears to me to provide is that in the case of the tender to the City of Toronto the 30-day limit provided in the agency contract is waived and the appellant is to have the right to pursue the matter to a conclusion but is to have a commission of $13.73 for each meter sold pursuant to the tender rather than the commission provided for in the agency contract. Such an alteration in my opinion has no effect on the income nature of the amount to which the appellant was to be entitled for his services as agent and the amount was accurately referred to as "commission" in the agreement of settlement. Nor, in my opinion, did the amount received by the appellant from A. M. I. Distributing Co. Ltd. in exchange for his right to such commissions, partake of any other character. I am quite unable to see what difference it can make that there was still a possibility that no commission would become payable. What the appellant had at the time of the assignment was a contingent right of an income nature. He exchanged it for $12,000 and a certain proportion of the commissions over that amount. If the City of Toronto had cancelled the purchase he would have been under obligation to return the $12,000 and any other sums which he had received in which case the receipts would have been offset by the deduction of what he would have had to repay. But this did not happen and I can see no reason why in the circumstances the amount received by the appellant should for income tax purposes be regarded as having a different nature from the income right which he exchanged for it. In respect of the sums of $12,000 and $1,470 in 1952 and $896.27 in 1953 received by the appellant from A. M. I. Distributing Co. Ltd., the appeal accordingly fails.

Turning now to the cross-appeal—because it arises out of the facts which I have been discussing—as previously mentioned this turns entirely on whether s. 16(1) of the *Income Tax Act* applies to render the 58 per cent. of the commissions retained by A. M. I. Distributing Co. Ltd. pursuant to the assignment agreement taxable as income of the appellant. This section provides that

> A payment or transfer of money, rights or things made pursuant to the direction of, or with the concurrence of, a taxpayer to some other person for the benefit of the taxpayer or as a benefit that the taxpayer

desired to have conferred on the other person shall be included in computing the taxpayer's income to the extent that it would be if the payment or transfer had been made to him.

It was argued that the payment of the commissions by Park-O-Meter of Canada Ltd. to A. M. I. Distributing Co. Ltd. was made pursuant to the direction of the appellant within the meaning of this subsection as a benefit which he desired to have conferred on A. M. I. Distributing Co. Ltd. In my opinion, s. 16(1) is intended to cover cases where a taxpayer seeks to avoid receipt of what in his hands would be income by arranging to have the amount received by some other person whom he wishes to benefit or by some other person for his own benefit. The scope of the subsection is not obscure for one does not speak of benefitting a person in the sense of the subsection by making a business contract with him for adequate consideration. Here, I see no reason to think that the 58 per cent. which A. M. I. Distributing Co. Ltd. was to retain was anything but the consideration for the risk which it took in paying out $12,000 to the appellant on the strength of a contract which might be cancelled and the mere liability of the appellant to repay it if that event occurred. In my opinion, s. 16(1) has no application to such a transaction and the cross-appeal accordingly fails.

There remains the issue respecting the $5,000 received by the appellant on the release of his right to 2½ per cent. on sales to be made after termination of the agency contract. As previously mentioned, the basis for the taxation of this sum put forward by the Minister in his reply was that it was received for the partial cancellation of an agency agreement entered into by the appellant in the course of his business. If the sum in question had in fact been received for the partial cancellation of the agency agreement, it would in my opinion be of the same nature as the $3,750 which, as already stated, I regard as a capital receipt.

But on the evidence, I do not think the sum can be said to have been received for the cancellation or the partial cancellation of the agency agreement. The 2½ per cent. was provided for in the first agreement and was to accrue only in the event of premature termination of the contract and then not on sales which the appellant might make but on sales which others might make after he had ceased operating. The nature of the appellant's right to such commissions in

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my opinion appears from the agreement of August, 1950, and the circumstances attending its execution. In that agreement, the consideration for these commissions is stated as "the introduction of McCowan to McGee-Hale, and the information and assistance already freely given and to be given by Miller to McCowan". The agreement is silent as to just what "the assistance already freely given" was, but it does appear that McCowan could not obtain the patent licence without the appellant's consent whether because McGee-Hale was protecting his position in that respect or because of McCowan's undertaking which is referred to in the second recital of the agency contract, not to negotiate with McGee-Hale for a period of five years, or both. Nor does it appear what was to be included in "assistance to be rendered". Provision was made in the agreement for commissions at specified rates for making sales of meters and so it appears to me that this is not included in the consideration for the 2½ per cent. commissions. The substantial consideration for the 2½ per cent. commissions, in my opinion, was the waiver by the appellant of his rights under the earlier agreement with McCowan and his consent to McCowan negotiating for a licence under the patent and this, I think, was the giving up by the appellant of a right of a capital nature in exchange for the right to the agency and the 2½ per cent. commissions. In this view, the right to such commissions was also a right of a capital nature whether or not the commissions when actually paid would have been income—a question which does not arise in these proceedings—and the $5,000 received by the appellant for the release of such right was also capital and not income. The appeal accordingly succeeds with respect to this item as well.

In the result, the appeal will be allowed with costs and the re-assessments varied to the extent indicated in these reasons. The cross-appeal will be dismissed with costs.

Judgment accordingly.

1961
Oct. 4
1962
July 27

BETWEEN:

IRVIN CHARLES SCHACTER .....APPELLANT;

AND

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

Revenue—Income Tax—Income Tax Act, R.S.C. 1952, c. 148, ss. 11(1)(a), 12(1)(a)(b)—Income Tax Regulations, Schedule B, Class 8—Purchase of accountant's business, goodwill and list of clients—Payment deductible under s. 12(1)(a) of the Income Tax Act—List of accounts not depreciable as a tangible asset.

Appellant, a chartered accountant practising in Winnipeg, by an agreement made in 1954 purchased from a retiring accountant "all the right, title and interest of the vendor in and to the goodwill of the accounting business" carried on by the vendor including the right to use the firm name. The agreement provided *inter alia* for the delivery by the vendor of a list of his clients showing the regular annual fees charged by the vendor for the usual annual audit and that the appellant should pay to the vendor as the price of such goodwill seventy per cent of the aggregate of the regular annual fees so charged. The seventy per cent amounted to $17,153.50 and this sum was paid by appellant who in computing his income for the year deducted it as an expense. The deduction having been disallowed by the respondent the appellant appealed claiming that the amount was an expense incurred for the purpose of gaining or producing income from his business and not an outlay of capital. Alternatively he claimed that he was entitled to a deduction of capital cost allowance in respect of the list of clients.

Held: That the expenditure was not of a recurring nature but was made once and for all with a view to bringing into existence an advantage for the long term benefit of the appellant's practice and was an outlay of capital deduction of which in computing income is prohibited by s. 12(1)(*b*) of the *Income Tax Act*.

2. That the goodwill for which the $17,153.50 had been paid was not a tangible capital asset within the meaning of the capital cost regulations made under s. 11(1)(*a*) of the *Income Tax Act* and that the appellant was not entitled to a deduction of capital cost allowance in respect of it. Nor was the appellant entitled to deduct capital cost allowance in respect of the list of accounts, as nothing had been paid for it and there was no capital cost of it to the appellant to which s. 11(1)(*a*) could apply.

APPEAL under the *Income Tax Act*.

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

C. V. McArthur, Q.C. for appellant.

A. J. Irving for respondent.

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

THURLOW J. now (July 27, 1962) delivered the following judgment:

In these proceedings the appellant appeals from a judgment of the Tax Appeal Board[1] by which his appeal from a re-assessment of income tax for the year 1955 was allowed in part and the Minister cross-appeals asking that the re-assessment be restored.

The controversy arises over a payment of $17,153.50 made by the appellant pursuant to an agreement which he had made with a Mr. Samuel Albert Portigal. In computing his income for tax purposes for a fiscal period which ended in February 1955 the appellant deducted the sum so paid as an expense but the Minister in making the re-assessment disallowed the deduction and the appellant thereupon appealed. In the Tax Appeal Board the disallowance of the $17,153.50 as a deduction was upheld but the Board sustained an alternative contention that the appellant was entitled to a deduction of capital cost allowance in respect of a list of accounts which the appellant had obtained in the transaction and accordingly allowed the appeal in part and referred the matter back to the Minister to make such an allowance.

The circumstances in which the payment was made were as follows. The appellant has been a chartered accountant since 1934 and since 1936 has practiced his profession at Winnipeg. In October 1954 he learned that Mr. Portigal, an accountant, who for some years had been carrying on accounting practice in Winnipeg under the firm name of George Loos & Co., was about to retire from practice, and he thereupon contacted Mr. Portigal and opened negotiations the purpose of which from the appellant's point of view was to increase his business by securing clients from Mr. Portigal's clientele. He had previously on two occasions purchased lists of accounts from retiring accountants but with some sort of guarantee from the vendor that the clients would stay with him. He could obtain no such commitment from Mr. Portigal but eventually he and Mr. Portigal made an agreement which was embodied in an indenture dated October 20th, 1954.

[1] 25 Tax A.B.C. 91.

By this it was recited that the vendor, Mr. Portigal had agreed to sell and the purchaser, the appellant, to purchase "all the right, title and interest of the Vendor in and to the goodwill of the accounting business" carried on by the vendor under said firm name and style of George Loos & Co., including the right to use the said firm name, on the terms and conditions thereinafter contained. The document went on in para. 1 to provide for such sale and purchase of the goodwill of the business, including the exclusive right to the use of the firm name effective from November 1, 1954 but to except the accounts of certain firms. In para. 2 it was agreed that "To facilitate the taking over by the Purchaser of said accounting business and the continuation of the accounting services by the Purchaser in the place of the Vendor," the parties would inform the clients that they were associating to carry on the accounting business and that for six months the vendor should not disclose to them that he intended to retire but that he should in the meantime upon request and without remuneration assist in completing their work for the year. At the end of six months or sooner if requested by the appellant, the vendor was to advise the clients of his retirement from the association and from the accounting business. The agreement also provided for delivery by the vendor to the appellant without remuneration of the vendor's records relating to the accounts "the goodwill relating to which has been hereby agreed to be sold and purchased" and for delivery of a list in duplicate of such accounts showing the regular annual fees charged by the vendor for the usual annual audit such list to be identified by the signatures of the parties and to be attached as a schedule and form part of the indenture. Para. 8 stated "So soon as such list of accounts shall have been agreed upon by the Parties hereto and identified by them and attached to this Agreement as aforesaid, seventy percent (70%) of the aggregate of said regular annual fees shown on said list shall then become the price to be paid by the Purchaser to the Vendor for the said goodwill". Subsequent paragraphs provided for collection by the appellant for the vendor without remuneration of the fees owing to the vendor, for a commission to be paid by the appellant on the fees from any new business which the vendor might refer to him and finally that the vendor would not engage in the business of accountancy within 400 miles of the City of Winnipeg for

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10 years except in connection with the work of some of the clients whose accounts had been excepted from the transaction.

The list referred to in the indenture was simply a three sheet list of 124 clients showing in separate columns amounts of fees for work done for the clients in 1953, the expected amounts of fees to be earned in 1954, which totalled $24,505, the amounts of unpaid accounts rendered for 1953 totalling $22,772.10 and the amounts of fees earned in 1954 to October 31, totalling $11,020.

In 1953 the vendor had lost his records in a fire and though he had later taken a new office the only records which he was in a position to turn over to the appellant were copies of certain financial statements which had been prepared by him for his clients and which had accompanied their income tax returns. The appellant did not occupy the office used by Mr. Portigal nor did he make use of the firm name of George Loos & Co.

As matters turned out a considerable number of Mr. Portigal's clients did not employ the appellant and by the end of the first year following the making of the agreement he had lost or failed to retain 41.3 per cent. of the dollar volume of the business. At the time of the trial however some seven years after the transaction he still retained 39 of the 124 clients and these accounted for 45 per cent. of the dollar volume of the business. As a result of the transaction and of the efforts which the appellant made to hold Mr. Portigal's former clients the income of his practice increased by about $10,000 per year and he found it necessary to engage two additional employees and to use more office space and consequently to pay a higher rent.

The 70 per cent. referred to in para. 8 of the indenture was calculated on the $24,505 shown on the list of accounts as the anticipated earnings for 1954 and amounted to $17,153.50. This amount was paid by the appellant to the vendor at the time of the execution of the indenture and the question to be determined in the appeal is whether it is properly deductible in computing income from the appellant's practice for income tax purposes.

The case for the appellant is that the $17,153.50 was an expense incurred for the purpose of gaining or producing income from his business which would on accepted accounting principles be deductible in computing the profit from

such business, that it was within the exception to the prohibition of s. 12(1)(*a*) of the *Income Tax Act* R.S.C. 1952, c. 148 and not within the prohibition of s. 12(1)(*b*) and was accordingly properly deductible in computing the appellant's income from his business for income tax purposes. The contention put forward on behalf of the Minister was that the expenditure was not an expense falling within the exception to s. 12(1)(*a*) and was moreover an expenditure of capital deduction of which was prohibited by s. 12(1)(*b*).

Subsections (*a*) and (*b*) of s. 12(1) provide:

> 12.(1) In computing income, no deduction shall be made in respect of
>
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer,
>
> (*b*) an outlay, loss or replacement of capital, a payment on account of capital, or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part,

In *B.C. Electric Railway Co. Ltd. v. M.N.R.*[1] Abbott J., speaking for the majority of the Court, after referring to the less stringent nature of the provisions of s. 12(1)(*a*) and (*b*) compared with the corresponding provisions of the *Income War Tax Act* said at p. 137:

> Since the main purpose of every business undertaking is presumably to make a profit, any expenditure made "for the purpose of gaining or producing income" comes within the terms of s. 12(1)(*a*) whether it be classified as an income expense or as a capital outlay.
>
> Once it is determined that a particular expenditure is one made for the purpose of gaining or producing income, in order to compute income tax liability it must next be ascertained whether such disbursement is an income expense or a capital outlay. The principle underlying such a distinction is, of course, that since for tax purposes income is determined on an annual basis, an income expense is one incurred to earn the income of the particular year in which it is made and should be allowed as a deduction from gross income in that year. Most capital outlays on the other hand may be amortized or written off over a period of years depending upon whether or not the asset in respect of which the outlay is made is one coming within the capital cost allowance regulations made under s. 11(1)(*a*) of *The Income Tax Act*.

On the facts of the present case I have no difficulty in reaching the conclusion that the expenditure in question was one that was made or incurred for the purpose of gaining or producing income from the appellant's business in the broad sense referred to by Abbott J. in the passage quoted and I therefore turn to the question whether it was an outlay of capital within the meaning of s. 12(1)(*b*).

[1] [1958] S.C.R. 133.

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In the same judgment Abbott J. continued at p. 137:

> The general principles to be applied to determine whether an expenditure which would be allowable under s. 12(1)(*a*) is of a capital nature, are now fairly well established. As Kerwin J., as he then was, pointed out in *Montreal Light, Heat & Power Consolidated v. Minister of National Revenue,* applying the principle enunciated by Viscount Cave in *British Insulated and Helsby Cables, Limited v. Atherton,* the usual test of whether an expenditure is one made on account of capital is, was it made "with a view of bringing into existence an advantage for the enduring benefit of the appellant's business".

This was reiterated in similar terms by the same Judge speaking for the Court in *M.N.R. v. Haddon Hall Realty Inc.*[1] at p. 110.

> The general principles to be applied in determining whether a given expenditure is of a capital nature are fairly well established: *Montreal Light Heat and Power Consolidated v. Minister of National Revenue; British Columbia Electric Railway Company Limited v. Minister of National Revenue.* Among the tests which may be used in order to determine whether an expenditure is an income expense or a capital outlay, it has been held that an expenditure made once and for all with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade is of a capital nature.

In the present case the expenditure in question was not of a recurring nature but one made once and for all and it also appears to me to have been made with a view to bringing into existence an asset or, perhaps more accurately, an advantage for the enduring benefit of the appellant's business. It is I think plain on the evidence that the expenditure was not made merely in the expectation of gaining additional business for the current year by securing the opportunity to complete Mr. Portigal's work for that year for such of the clients as would permit the appellant to do so. Had that been the purpose there would have been no occasion for a restrictive covenant of ten years duration. Moreover the size of the amount paid in comparison with that of the vendor's annual gross revenue appears to me to preclude such a conclusion for it was greater than the expected gross revenue for the remainder of the year, probably greater than the net revenue for a full year and in view of the fact that the appellant could scarcely hope to retain all of the clients, probably greater by an even larger amount than the net revenue which the appellant could expect to obtain from the clients in any single year. In my view what the appellant sought to obtain by making

[1] [1962] S.C.R. 109.

the agreement and paying the sum in question was the long term benefit of an expansion of his own clientele and the various provisions of the indenture were directed to enable him to achieve this expansion through the transfer to him of such of the goodwill attaching to Mr. Portigal himself and to the name of George Loos & Co. as could be retained on Mr. Portigal's retirement from practice. And while the actual retention of the clients must have depended to a great extent on his own ability and efforts to win and hold their confidence the size of the amount he was prepared to pay for such goodwill as Mr. Portigal could transfer to him and the fact that some seven years after the transaction he still retained a substantial number of the clients with a substantial proportion of the volume of their business in my opinion shows the long term or enduring nature of the advantage which he sought to obtain.

To my mind the enduring quality of the advantage sought also appears from the transfer of the right to use the name of George Loos & Co. which, though the appellant never used or intended to use the name, permanently prevented Mr. Portigal from using it or transferring his right to use it to any competitor who might thereby attract clients which Mr. Portigal had served.

Applying the test referred to in the passages cited from *B.C. Electric Railway Co. Ltd. v. M.N.R.* and *M.N.R. v. Haddon Hall Realty Inc.* these considerations suggest that the expenditure in question was of a capital rather than of a revenue nature. Nor do I see in the circumstances any special features pointing to an opposite conclusion. On the contrary the conclusion which it suggests appears to me to be indicated as well by the fact that the expenditure was not an ordinary incident of the appellant's day to day practice and by the terms of the document pursuant to which the payment was made. The indenture refers to the transaction as a sale of the goodwill of the vendor's business including the exclusive right to use the firm name of George Loos & Co. and it will be recalled, specifically identifies the sum in question as the price to be paid for such goodwill. It is true that the document also required the vendor to render certain services for which no separate consideration or part of the sum in question was particularly assigned but to treat the sum as paid in whole or in part

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for such services would appear to be contrary to the express provision of the agreement. Moreover while the vendor's services were to be rendered "without remuneration" so also were the services to be rendered by the appellant in collecting the vendor's accounts amounting to some $33,000 and in view of these mutual and somewhat complementary undertakings, affording as they do some consideration in fact for one another, I do not think a conclusion that the sum in question was paid for anything but what the document expressly provides for would be warranted. It may be conceded that not every expenditure which may have the effect of increasing the goodwill of a business is necessarily one of a capital nature but to my mind the fact that in the present case the sum in question was the consideration for the purchase of the goodwill of an established undertaking suggests that it was an outlay of capital rather than an expenditure on revenue account. *Vide Associated Newspapers Ltd. v. Federal Commissioner of Taxation*[1] where Latham, C.J., said at p. 91:

> The effect of the payment was to enlarge the goodwill of the enterprise, which was one of its most valuable assets. There is no doubt that the goodwill of the Sun newspaper became worth very much more as the result of the agreement which prevented the publication of a competitive newspaper within the same area, possibly at a lower price, by persons who had the control of a press and the necessary plant, together with a newspaper organisation in being. In the case of *Anglo-Persian Oil Co. v. Dale,* reference was made by *Lawrence,* L.J., to the fact that in that case the company by making the payment in question did not improve its goodwill. So also in *Nevill v. Federal Commissioner of Taxation,* reference is made to the increasing of the value of the goodwill of a company as a relevant circumstance, at p. 303:—"enlargement of the goodwill of a company" and at p. 306:—"permanent improvement in the material or immaterial assets of the concern". The goodwill of a business is an asset of the business and is plainly a capital asset. It is radically different from assets which are turned over and bought and sold in the course of trading operations.

Nor in my view is the matter affected by the fact that goodwill in the case of an accountant and particularly one who practices alone is largely personal to the particular practitioner and scarcely capable of being sold with any assurance that the purchaser will obtain any benefit from it. No doubt one who pays for so tenuous an advantage takes a risk but there is nothing uncommon about professional men acquiring the undertakings of established practitioners with whatever goodwill can be retained in the

[1] 5 A.T.D. 87.

transfer and I know of no reason why if they see fit, as appears to have occurred in this case, they cannot in such a transaction agree upon a consideration for such goodwill. The fact that in the result no goodwill may be acquired or that the benefits of the purchase may soon disappear appears to me to be irrelevant for the present purpose for in the test referred to in the cases cited what matters is the nature of the advantage sought rather than the benefit actually obtained.

Accordingly I am of the opinion that the expenditure in question was an outlay of capital the deduction of which in computing income for income tax purposes is prohibited by s. 12(1)(*b*). The appeal therefore fails.

There remains the cross-appeal against that part of the judgment of the Tax Appeal Board which holds the appellant entitled to a deduction of capital cost allowance under Class 8 of Schedule B of the *Income Tax Regulations* in respect of the value of the list of accounts which the appellant acquired in the transaction in question. The reasons for so holding were thus expressed in the decision of the Board:

> As I am of the opinion that by far the larger part of the purchase price of the list of accounts was paid for whatever goodwill existed in connection with the clients who were purportedly being turned over by Mr. P to the appellant herein, this was therefore a capital expense which is not allowable as a deduction from income as claimed by the appellant. However, some small part of the purchase price was represented by the list of accounts turned over by Mr. P. to the appellant herein, and those accounts, in my opinion, constituted a tangible asset of the appellant which would be subject to capital cost allowance under the Income Tax Regulations. I leave the determination of the amount representing the value of this list for the consideration of the Minister, as I have no evidence on which to base even an estimate of the value of the said list of accounts.
>
> In the circumstances, the appeal is allowed in part, and the matter is referred back to the respondent for him to determine the value of the list of accounts paid for by the appellant upon which capital cost allowance under Class 8 of Schedule B of the Income Tax Regulations may be afforded.

In this court the position taken by the appellant was that if the sum paid was not deductible as an expense, the list of accounts which the appellant obtained in the transaction was a tangible capital asset depreciable at the rate of 20 per cent. under Class 8 of the *Income Tax Regulations*. The Minister's submission was that no tangible capital asset was acquired in the transaction and that no part of the outlay was subject to capital cost allowance.

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Section 11(1)(*a*) of the *Income Tax Act* provides as follows:

11. (1) Notwithstanding paragraphs (*a*), (*b*) and (*h*) of subsection (1) of section 12, the following amounts may be deducted in computing the income of a taxpayer for a taxation year:

(*a*) such part of the capital cost to the taxpayer of property, or such amount in respect of the capital cost to the taxpayer of property, if any, as is allowed by regulation;

The regulation invoked by the appellant in support of his contention reads: (1955 Canada Gazette, Part II, 1954-1917).

1100.(1) Under paragraph (*a*) of subsection (1) of section 11 of the Act, there is hereby allowed to a taxpayer, in computing his income from a business or property, as the case may be, deductions for each taxation year equal to

(*a*) such amount as he may claim in respect of property of each of the following classes in Schedule B not exceeding in respect of property

(1)—(vii) . . .

(viii) of class 8, 20%,

(ix)—(xv) . . .

Class 8 is defined as:

Property that is a tangible capital asset that is not included in another class in this Schedule except land, or any part thereof or any interest therein, and also excepting

(*a*) an animal,

(*b*) a tree, shrub, herb or similar growing thing,

(*c*) a gas well,

(*d*) a mine,

(*e*) an oil well,

(*f*) radium,

(*g*) railway track,

(*h*) railway grading,

(*i*) a railway subway,

(*j*) a railway street crossing,

(*k*) a right of way,

(*l*) timber limit, and

(*m*) tramway track.

The *Shorter Oxford English Dictionary*, 3rd Edition, revised 1956, gives the following definitions of "tangible":

(1) Capable of being touched, affecting the sense of touch; touchable. Hence, material, externally real, objective.

(2) That may be discerned or discriminated by the sense of touch, as a tangible property or form.

(3) That can be laid hold of or grasped by the mind, or dealt with as a fact; that can be realized or shown to have substance.

In Funk & Wagnall's *New Standard Dictionary of the English Language* (1961) "Tangible" is defined as meaning:

(1) Perceptible by touch, also within reach by touch.

(2) Figuratively, capable of being apprehended by the mind; having definite shape; not elusive or unreal.

(3) Perceptible to the senses; corporeal; as tangible property; opposed to incorporeal property such as franchises.

In number (3) of the *Shorter Oxford English Dictionary* definitions and number (2) of the Funk & Wagnall definitions the meaning appears to be broad enough to include incorporeal concepts as well as corporeal objects. However in *Accounting Terminology*, a volume published in 1957 by the Canadian Institute of Chartered Accountants, the definition given for "tangible assets" and "tangibles" is:

All assets except the intangible assets such as goodwill, patents, copyrights, trademarks.

In my opinion the nearest of the definitions to the meaning of "tangible" as used in the definition of Class 8 of the regulations is number (3) of the Funk & Wagnall definitions and I do not think that either goodwill or "accounts" constitute "a tangible capital asset" within the meaning of that expression in the regulation. The contention was however made that the list of accounts is itself tangible property in respect of which capital cost allowance may be claimed. The answer to this in my opinion is that on the evidence there was no capital cost of the list to the appellant within the meaning of s. 11(1)(*a*) in respect of which a capital cost allowance may be made. The whole of the $17,153.50 was paid for goodwill. The list was not goodwill but was simply a document prepared by Mr. Portigal which in the course of the transaction became a schedule to and part of the indenture. It was not sold to the appellant and nothing was paid by the appellant for it. The cross-appeal accordingly succeeds.

In the result therefore the appeal will be dismissed with costs and the cross-appeal will be allowed with costs and the re-assessment restored.

Judgment accordingly.

1961
Sept. 27
1962
Aug. 17

BETWEEN:

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

AND

MAX WOLFE ..... RESPONDENT.

Revenue—Income tax—The Income Tax Act, 1948, S. of C. 1948, c. 52, ss. 3, 4, and 127(1)(e)—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, and 139(1)(e)—Bonus on mortgages—Mortgage discounts—Capital gains or income—Taxpayer engaged in speculative or adventurous undertakings in nature of trade—Appeal allowed.

Respondent, engaged in the wholesale produce business, from time to time purchased mortgages recommended to him by his solicitor at a discount and also made direct loans to mortgagors receiving a bonus on such. All these mortgages were for short terms and most were second mortgages on real property, some were second chattel mortgages. The Minister of National Revenue assessed the respondent for income tax on the discounts and bonuses realized on 31 of these transactions for the years 1948 to 1953 inclusive. An appeal to the Tax Appeal Board was allowed and from that decision the Minister appeals to this Court.

Held: That the discounts and bonuses realized by the respondent are income and subject to tax.

2. That while the respondent could not be said to be operating a business in the ordinary sense of the term he was engaged in speculative or adventurous undertakings of a trading nature within the provisions of s. 139(1)(*e*) of the *Income Tax Act*.

3. That respondent's mortgage dealings were short-term profit-making transactions frequently repeated, highly speculative and could not be regarded as ordinary or normal investments.

APPEAL under the *Income Tax Act*.

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

H. D. Guthrie, Q.C. for appellant.

J. J. Robinette, Q.C. for respondent.

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

KEARNEY J. now (August 17, 1962) delivered the following judgment:

The Court is here concerned with an appeal from a decision of the Income Tax Appeal Board reported as *No. 565* v. *The Minister of National Revenue*[1], wherein the

[1] 20 Tax A.B.C. 158.

respondent's (hereinafter sometimes referred to as "the taxpayer") appeal from reassessments of his income tax for the years 1948 to 1953, inclusive, was allowed.

In his reassessments, the appellant added to the respondent's reported income, for each of the above-mentioned years, the sums of $9,225, $1,790, $1,570, $7,950, $4,350 and $4,250 respectively, representing either bonuses or discounts received by the taxpayer in respect of direct loans which he made to mortgagors or discounts on mortgages which he purchased.

The case turns on whether the foregoing amounts constitute income from a business within the meaning of s. 3 of *The Income War Tax Act,* R.S.C. 1927, ss. 3, 4 and 127(1)(*e*) of the *Income Tax Act,* S. of C. 1948, c. 52, and ss. 3, 4 and 139(1)(*e*) of the *Income Tax Act,* R.S.C. 1952, c. 148.

Although the taxpayer, in the first year in question, was assessed under *The Income War Tax Act,* in the later years under the *Income Tax Act 1948,* and still later, under the present Act as contained, for the purposes of the present appeal, in the 1952 revision, counsel agreed that nothing turns on this differentiation and that we may direct our attention solely to the *Income Tax Act* as it stood in 1952, the relevant provisions of which 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)(*e*). 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.

At the opening of the hearing, counsel for the appellant tendered as exhibits the returns filed by the taxpayer for the six years in question, the Minister's reassessment for each of such years, the taxpayer's notices of dissatisfaction and the Minister's replies thereto, which, by consent, were filed as a single exhibit marked "Ex. 1". Similarly, a

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memorandum, containing fifteen consecutively numbered pages, plus four additional pages some of which are unnumbered and hereinafter referred to as a supplement, giving, *inter alia*, particulars and the number of each mortgage transaction entered into by the respondent during the six years in question, as well as similar transactions effected by the taxpayer in years prior and subsequent to the 6-year period in question, was filed as Exhibit 2.

The only witness heard on behalf of the respondent was the taxpayer himself.

At the date of trial, he was in his 70th year. Born in Warsaw, he came to Canada in 1905. He resides in Forest Hill Village, Toronto, where he has been "for many, many years engaged in the fruit and vegetable business". From a modest beginning, he caused to be incorporated in 1911 the Ontario Produce Company, of which, at the time of the hearing, he was vice-president, owning 50 per cent of the issued stock of the company, his brother being the owner of the other 50 per cent. He held a similar office and stock ownership in Oshawa Wholesale Limited, which was a distributor of fruits and vegetables to the IGA stores and groceries. Prior to 1930 the respondent had been able to effect savings which he invested in the stock market and which he totally lost following the 1929 crash.

Since the above loss, the respondent, as he modestly put it, has been able to buy some odd few shares of stock as the money came to him. I say "modestly" because the schedules of his dividends attached to his income tax returns show that during the six years in issue his average dividends from his stock market investments have amounted to about $10,000 per annum.

In respect of mortgage transactions, leaving aside the interest he derived therefrom, the respondent's average realization on discounts and bonuses during the same period amounted approximately to $5,000 per annum. His evidence also indicates that he attended to his own stock market investments and these show very little variation from year to year. The respondent does not appear to have invested in bonds but very largely in what are sometimes termed "growth stocks", consisting of dividend yielding common shares.

Any time the question of putting his money into mortgages arose, Mr. Wolfe relied entirely on Mr. Shifrin who was his nephew and legal adviser. The respondent stated that he was wholly occupied from early morning to late at night in his fruit and vegetable business and had neither the time nor the required knowledge to appraise the worth or otherwise of the mortgages which he acquired through his legal adviser. He testified that he did not see or interview any of the mortgagors nor did he inspect any of the properties on which his mortgages were to be registered. Whether he acquired a mortgage recommended by his legal adviser only depended on whether he happened to have sufficient funds on hand to pay for it. Incredible as it may seem, he stated that he did not even enquire about the rate of interest nor whether he was entitled to any bonus or discount. Mr. Shifrin made the collections, attended to necessary insurance and had possession of all documents in connection with the mortgages.

The following is a cumulative copy of Schedule "A" which is attached to each reassessment made by the Minister for the six-year period in question in respect of the 31 mortgages which are in issue. The last column shows the amounts which he added to the respondent's taxable income in each of the six years, and, for ready reference, I have taken the liberty of adding a first column indicating the number which has been assigned in exhibit 2 to each mortgage transaction mentioned therein.

MINISTER'S SCHEDULE "A" FOR THE YEARS 1948 TO 1953, INCLUSIVE

No. (Ex. 2)	*Mortgagor*	*Type of Mortgage*	*Mortgage Face Value*	*Max Wolfe Share*	*Max Wolfe Share of 1948 Profits*
		1948			
50	Brittania Hotel	2nd	$16,200.00	All	$1,500.00
63	Windsor Hotel	2nd	5,000.00	All	600.00
48	Autoguild Motors	2nd	8,800.00	All	800.00
40	Dominion Hotel	2nd	8,500.00	All	400.00
50	Brittania Hotel	3rd	22,000.00	All	3,000.00
Supp., p. 2	Governor Simcoe Hotel Ltd.	2nd	31,000.00	½	2,500.00
"	Repath, T. B. and A. V.	2nd	2,400.00	½	125.00
47	Andrews, Marie	2nd	1,500.00	All	300.00
					$9,225.00

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No. (Ex. 2)	Mortgagor	Type of Mortgage	Mortgage Face Value	Max Wolfe Share	Max Wolfe Share of 1948 Profits
		1949			
37	Anthony-Wilkie-York	2nd	$ 4,978.00	All	$ 600.00
41	Gamble, Gertrude C.	2nd	2,500.00	All	250.00
42	Gunning-Mason	2nd	2,140.00	All	140.00
40	Dominion Hotel	2nd	3,200.00	All	400.00
33	Rochester House	2nd	* 10,200.00	All	400.00
	* November 1, 1948—Cancelled January 1949.				$1,790.00
		1950			
27	Grand Trunk Hotel	2nd	$ 7,000.00	All	$ 500.00
34	Sieverling, P. & A.	2nd	2,350.00	All	220.00
25	Dutch Inn	2nd	6,350.00	All	550.00
32	Raxlen-Lewis	2nd	5,500.00	All	300.00
					$1,570.00
		1951			
22	Oakville House	2nd	$14,200.00	All	$1,450.00
26	Richelieu Hotel	2nd	15,000.00	All	3,000.00
20	Jasper Hotel	2nd	10,000.00	All	1,750.00
24	Bright House	2nd	17,500.00	All	1,750.00
					$7,950.00
		1952			
11	Lowe-Secord	2nd	$ 2,350.00	All	$ 500.00
6	Davidson-Browning	2nd	1,400.00	All	350.00
15	Quinte Hotel	2nd	29,000.00	All	3,000.00
14	Piskor-Lane	2nd	4,250.00	All	500.00
					$4,350.00
		1953			
9	Lewis, David	2nd	$ 1,900.00	All	$ 200.00
12	Norris, H. R.	2nd	7,000.00	All	900.00
2	Baldwin, A. H.	2nd	2,500.00	All	250.00
4	Calder, Charles	3rd	2,000.00	All	500.00
16	Tabone, Harry	2nd	5,500.00	All	1,400.00
Supp., Downey, Thomas and Mary p. 4		2nd	3,600.00	All	1,000.00
					$4,250.00

Besides assigning a particular number to each transaction Exhibit 2 gives further information regarding the 31 mortgages in issue as described in the aforementioned Schedule, e.g., it distinguishes chattel mortgages from other mortgages; indicates the rate of interest on each mortgage and how it is payable; the manner in which the principal is repayable; the life or duration of the mortgage; and whether the taxpayer obtained a bonus or discount in respect thereof.

I do not think it necessary to put on record the above-mentioned further particulars in respect of all the mortgage transactions of the taxpayer between 1948 and 1953, but the following graph sets out such particulars in respect of the year 1948, being the one in which the respondent's mortgages, both numerically and in amount, were larger than any other subsequent year. I have inserted, after the figures under the title "Discount or bonus", the letter (b) or (d) to indicate under which of the two categories the figure falls.

No. (Ex. 2)	*Mortgagor*	*Face value and type*	*Discount or Bonus*	*Duration*	*Rate of interest*	*Repayment a/c of principal*
50	Brittania Hotel	$16,200 2nd chattel	$1,500(b)	Apr. 22/46 " ?/48	8% per an. payable monthly	$300 monthly
63	Windsor Hotel	$ 5,000 2nd	600(b)	Apr. 1/46 " ?/48	8% "	$125 monthly
48	Autoguild Motors	$ 8,800 2nd	800(d)	Apr. 13/47 " 13/48	10% "	$400 monthly
40	Dominion Hotel	$ 8,500 2nd	400(b)	July 1947 Aug. 1948	?	$200 monthly
50	Brittania Hotel	$22,000 3rd chattel	300(b)	Oct. 1947 Aug. 1/48	5% "	$150 monthly
*Governor Simcoe Hotel Ltd. (See Ex. 2—Supplement, p. 2)		$31,000 2nd chattel	$5,000(b)	Oct. 31/47 Dec. 9/48 (assigned)	5% "	$800 monthly
47	Andrews, Marie	$ 1,500 2nd	300(b)	Jan. 30/48 Nov. ?/48	5% "	$ 50 monthly
*Repath, T. B. and A. V. (Supplement, p. 2)		$ 2,400	250(b)	Feb. 20/48 Dec. 15/48 (assigned)	5% "	$150 monthly

*These chattel mortgages were held by Max Wolfe and his brother Maurice in equal shares and were assigned by the holders to Ontario Produce Co. Limited, the assignors receiving full amount owing at that time, namely, $20,600 and $1,650 respectively.

As appears on Exhibit 2, page 1 of the Supplement, the respondent and his brother made assignments similar to those above-mentioned in respect of earlier first mortgages which are not in issue.

The following is what I might term a combined analysis of Exhibit 2 made in argument by counsel for the parties, which, except in one instance—I will refer to it later—, I find to be substantially accurate.

During the aforementioned 6-year interval all of the 31 mortgages fell due or were realized. The great majority of the mortgages represented direct loans to the mortgagors

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in respect of which the respondent received a bonus and the remainder was purchased by the taxpayer at a discount. According to my count, 22 of them were 2nd mortgages on real property, one was a 3rd mortgage on realty, seven were 2nd chattel mortgages and one was a 3rd chattel mortgage on hotel furnishings and equipment. Sixteen of them bore interest at 5 per cent, one at 5½ per cent, eight at 6 per cent, two at 8 per cent and one at 10 per cent. No rate of interest is mentioned as regards one of the two Dominion Hotel mortgages.

The period from the acquisition by Mr. Wolfe of the mortgages to maturity, either by purchase or by an original direct loan to the mortgagor, ranged from one to five years, nine of them matured in less than two years, twelve in two years and five in more than two but less than five years. It was necessary for the respondent in the case of six of the said mortgages to extend the due date thereof for one year, at which time they were paid by the mortgagor. Mr. Wolfe was the sole proprietor of 29 of the said 31 mortgages and shared a 50 per cent interest with his brother Maurice in the other two. Between 1937 and 1945 his mortgage investments consisted exclusively of 1st mortgage transactions, which were 19 in number, bearing interest from 5 to 7 per cent, but the great majority of them yielded 6 per cent and in no case was any discount or bonus involved. Apparently in 1946 the respondent first became interested in 2nd mortgages and acquired eleven of them during 1946 and 1947. Counsel for the respondent considered that, among the 31 mortgages with which we are concerned, the maturity date of ten of them was five years, and this statement gives rise to the aforementioned instance which I think calls for some detailed consideration and consequent modification.

In perusing Exhibit 2, which contains some obvious typographical errors and omissions, I found one mortgage transaction (Anthony-Wilkie, No. 37) in which the principal fell due in something over three years; the Jasper Hotel mortgage (No. 12) fell due in a little over two years; and the same was true in connection with No. 15, The Quinte Hotel. But I was only able to discover five instances in which a 5-year term was mentioned.

The first of the said five transactions was the Lowe-Secord mortgage (No. 10—Ex. 2), which was assumed by Enrico Carfagnini and dated August 29, 1947, maturing August 30, 1952. It was assigned to Max Wolfe on September 12, 1947 at a discount of 500 and was discharged on September 23, 1952—but this appears to be the only instance in which the respondent held a 5-year mortgage to maturity.

The said five transactions were as follows:

The Grand Trunk Hotel mortgage was dated December 30, 1947 and matured on December 16, 1952.

The Davidson-Browning mortgage (See Ex. 2—No. 6), which was dated January 15, 1948, maturing in five years, was assigned to Max Wolfe with a discount of $350 on February 23, 1948, and discharged on May 1, 1952, or eight months and a half prior to the date of its maturity.

The Charles Calder transaction concerns a $2,000 3rd mortgage for five years (Ex. 2—No. 4) dated April 1, 1952. It was assigned to Max Wolfe on August 11, 1952 and reassigned by him on July 11, 1953 to Ontario Produce Co. Limited, at which time there was $1,900 owing on it, and as appears by a pencilled notation, Max Wolfe received full payment of this sum.

Re Downey (See last page of Supplement—Ex. 2). This was a 5-year mortgage for $3,600 dated February 16, 1953. The mortgagee was Gordon I. Gonthier, who assigned it to Max Wolfe on March 5, 1953 at a discount of $1,000, who in turn reassigned it on June 16, 1953 to Ontario Produce Co. Limited, which paid to Max Wolfe the amount then owing on the said mortgage, viz., $3,571.44.

I now pass on to consideration of the evidence given by the two witnesses heard on behalf of the appellant. Mr. John S. MacLeod, Assistant Treasurer of The Toronto General Trusts Corporation, who had charge of mortgages, stated that his company only invests in 1st mortgages to the extent of 60 per cent of the mortgage lending value of the property concerned, as provided in *The Trustee Act* of Ontario. The prevailing rate of interest from the early 1940's until 1951 was 5 per cent. During that year and until mid-1954 it varied between 5 and 5½ per cent. Shortly thereafter it rose to 6 per cent, where it remained until 1956. At the time of hearing it was 7 per cent. Mr. MacLeod added

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that, although the Trust Company with which he is connected does not deal in 2nd mortgages, he had occasion to observe that in the Toronto area substantial investments were made in 2nd and 3rd mortgages and that it was not uncommon for the mortgagee, in addition to a rate of interest which corresponded with the going rate on 1st mortgages, to ask for a bonus or discount, and, in instances where the money was borrowed to provide part of a purchase price, it was normal investment practice to do so.

While Mr. MacLeod's testimony, particularly on cross-examination in respect of investment practice, indicates that individuals in need of money frequently borrowed on 2nd mortgages, it does not throw any light on what was the status or business of the grantors of mortgages concerned, or whether it was customary for such individuals not publicly engaged in the business of lending to deal in them to the extent to which the respondent did, nor does it take into consideration the respondent's even more speculative dealings in chattel mortgages.

Reginald F. Heal, who for 30 years was engaged in the Real Estate and Mortgage Brokerage business in Toronto, was next heard on behalf of the appellant. The witness stated that he had dealt in 2nd mortgages by obtaining them for clients in need of money and then disposing of them to would-be purchasers. He stated that while each 2nd mortgage loan had to be judged on its own merit, in respect of prevailing interest rates from 1946 to 1950, when 1st mortgages were yielding 5 or 5½ per cent, 2nd and 3rd mortgage rates would be between 2 or 3 per cent higher. On temporary building loans 2 per cent per month was a common rate.

Speaking of discounts and bonuses, he said they occurred in both 1st and 2nd mortgages, and, when added to the interest rate in the case of 2nd mortgages, the calculated yield, depending on the security and how pressing was the need of the borrower, would be as high as 12 per cent. He rarely dealt in chattel mortgages because of the "terrific risk" involved, and in respect of 2nd chattel mortgages the interest charges, he stated, could be ridiculously high.

On cross-examination Mr. Heal testified that between 1948 and 1953 it was normal practice for investors to demand a discount on 2nd and 3rd mortgages, and this was sometimes true of 1st mortgages, particularly when "the

principal was higher in relation to the value of the property." In 98 per cent of such cases a person who wanted to sell a 2nd mortgage could not do so unless he gave a discount off the principal.

The issue with which we are here concerned has been commonly described as a *capital gain* or *income* case—and the following are four most recent decisions which are reported in the current edition of the 1962 Canadian Tax Cases and which, together with the authorities therein referred to, comprise a very complete review of what has been so far said on the question in issue: *Minister of National Revenue* and *Minden*[1]; *Irrigation Industries Ltd.* and *Minister of National Revenue*[2]; *Minister of National Revenue* and *MacInnes*[3]; *Minister of National Revenue* and *Rosenberg*[4]. The said jurisprudence indicates a sometimes divergent approach to the subject which I think illustrates the appositeness of what was said more than half a century ago in the oft-quoted case of *Californian Copper Syndicate v. Harris*[5], wherein Lord Justice Clerk observed:

> 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?

I propose to examine the question of the applicability to the case at bar of the various helpful tests or indicia referred to in the above-mentioned jurisprudence with a view to determining whether or not it can be said that the respondent was engaged in an *adventure in the nature of trade.* In the first place, I believe that, in a case such as this, the word "adventure" is, to all intents and purposes, synonymous with speculation and risk. The securities in issue certainly could not be regarded as approved investments under *The Trustee Act,* R.S.O. 1950, c. 400 (as amended), and I believe the same may be said of the corresponding acts of the other provinces. The evidence shows that six mortgagors could not pay their mortgage when it fell due but that after being granted a delay of a year they were able to do so.

[1] [1962] C.T.C. 79 at 91.
[2] [1962] C.T.C. 215.
[3] [1962] C.T.C. 350.
[4] [1962] C.T.C. 372.
[5] 5 T.C. 159 at 166.

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The evidence clearly shows the respondent not only agreed to accept ordinary second mortgages as security but also risked large sums, I would not say on the strength, but rather on the weakness of chattel mortgages.

Mr. Heal, whose business includes transactions in 2nd mortgages, stated that, beyond having an odd chattel mortgage, he did not deal in them "because you would have to be a great gambler to take one"; and the witness added that he had never heard of such a thing as a 2nd chattel mortgage. The evidence shows that the respondent, in respect of the year 1948, after allowing for the discounts and bonuses which he had received, had made a so-called investment of $15,875 in four ordinary 2nd mortgages and over $55,000 in 4 chattel mortgages, three of which were 2nd chattel mortgages and the other was a 3rd chattel mortgage, which, in my opinion, shows that the adventurous nature of the said transactions is established beyond question.

Counsel for the respondent, relying on the evidence of Mr. MacLeod, submitted that, unlike, for instance, the case of *Minister of National Revenue v. Spencer*[1], there was evidence in the present case establishing that the mortgages in issue constituted usual or normal forms of investment.

The chattel mortgage transactions above described added to the frequent acquisitions of 2nd mortgages, in my opinion, serve to give to the respondent's entire mortgage dealings an extraordinary speculative character which, I think, removes them from the category of what is regarded as normal or ordinary investments.

Another factor often referred to is the matter of relationship between the taxpayer's ordinary occupation and his mortgage dealings. I think this facet of the case should be resolved in favour of the taxpayer because the evidence indicates that no significant relationship of this nature existed.

As I read the jurisprudence, a most important, if not the most telling test referred to, concerns the repetitious nature of short term quick profit making transactions. In contrast to his portfolio of stocks which varied very little during the six-year period in question, his mortgage investments cannot, on the evidence, be regarded otherwise than as of

[1] [1961] C.T.C. 107.

very short duration, accompanied by a system of frequent replacements. As Kerwin J. (as he then was) observed in *Noak* and *Minister of National Revenue*[1], "the number of transactions, and, in some cases, the proximity of the purchase to the sale, indicates the carrying on of a business."

What was said by Kerwin J. in respect of sales of securities is equally applicable when they are converted or realized upon. See Kellock J. (*supra*) at p. 138. At page 139, this learned judge concluded by saying that in the case in question he concurred with the learned trial judge "in the view that the appellant has not satisfied the onus of establishing any error in the method of assessment and would dismiss the appeal with costs."

The respondent stated that he never sold any of his 2nd mortgages. I do not question his good faith in saying this, but in strict point of fact it is not so because, as I have already indicated, he made assignments of such mortgages to Ontario Produce Co. Ltd. and did not pass on to the Company any part of the bonuses or discounts which he had obtained; he thus received full payment of the amount outstanding thereon. It is true that he and his brother owned and controlled the last-mentioned Company, but from the point of view of taxation the Company and the respondent were distinct entities. These above-mentioned occurrences, while not overly important in themselves, are just what one would expect to find where a person was engaged in the business of lending money or a scheme for profit-making.

The respondent testified that he never resorted to advertising in connection with his mortgage transactions—and whether or not Mr. Shifrin did, he did not know.

Neither did he have recourse to borrowing in order to make possible his acquisitions in mortgages: He did so out of his savings—and, insofar as these criteria may constitute a factor, his evidence in respect of them would operate in his favour.

Another important indicia is the proof of the taxpayer's intent in entering into the transactions which he did. Whether the respondent was attracted to the ventures upon which he embarked was because of the profit he would make

[1] [1953] 2 S.C.R. 136 at 137.

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or the interest he would receive, or a combination of both, we will never know, since, on his own evidence, due to lack of knowledge, he was incapable of forming any intent. The President of this Court, in the *Minden* case (*supra*), held that the fact that the taxpayer knows nothing about his mortgage investments cannot exempt him from responsibility for the conduct and acts of his agent. But here again, the Court is left in the dark, because Mr. Shifrin, in whom the taxpayer had implicit confidence, was not called as a witness. Insofar, therefore, as intent is concerned, it is to be determined by the inferences to be drawn from the nature of the transactions—and I consider that the proof on this score weighs heavily against the respondent.

To what extent, if any, can it be said that the respondent organized himself in order to carry out the transactions in issue?

Apart from sharing a 50 per cent interest with his brother Maurice in the Brittania Hotel and The Governor Simcoe Hotel mortgages, he was the sole party having any interest in the remaining transactions. The only thing, in this case, which might savour of organization was Mr. Shifrin's status in the case. That a considerable amount of administrative work fell on Mr. Shifrin's shoulders appears from the fact that replacement of mortgages was frequent and all of them bore interest on a monthly basis or a quarterly basis, and the same is true with respect to repayments on account of capital. No evidence was offered with respect to the contractual relationship between Mr. Wolfe and Mr. Shifrin and I do not think that any important deductions, one way or the other, can be drawn under this heading.

In my opinion, on balance the evidence in this case, while it likely falls short of establishing that the respondent was engaged in operating a business in the ordinary sense of the term, it nevertheless proves he was engaged in speculative or adventurous undertakings of a trading nature within the extended meaning of the word "business" as contained in s. 139(1)(*e*) of the Act.

For the reasons above-mentioned I find in favour of the appellant and I would allow the Minister's appeal herein with costs.

Judgment accordingly.

ONTARIO ADMIRALTY DISTRICT

1961
April 10, 11
12, 13

BETWEEN:

CANADIAN BRINE LIMITED .....PLAINTIFF;

1962
July 26

AND

THE SHIP *SCOTT MISENER* AND HER OWNERS ..... } DEFENDANT.

Shipping—Damage to pipeline caused by negligence of defendant ship—Interest allowed as part of damages.

The action is brought to recover damages suffered by the plaintiff which serviced, repaired and maintained a portion of a pipeline running from Windsor, Ontario to Detroit, Michigan under the Detroit River. The pipeline was damaged by one of the flukes of an anchor of the defendant ship. The defendants admitted that the anchor fouled a portion of the pipeline in the vicinity of the place of anchorage but contend that such fouling was without negligence and that the ship was forced to anchor where it did due to weather conditions and the visibility at the time and also that it was necessary to use both bow and stern anchors due to a heavy down current and ice conditions. The plaintiff pleads negligence, trespass and nuisance.

The Court found that the captain of the defendant ship anchored it without any care or regard to any signs which might be available to him which would indicate that he was anchoring in an area where he might do serious damage, and without regard to the rights of others in that area. It was also negligence on the part of the officers of the defendant ship to direct that the anchor be raised and lowered until the obstruction which it had picked up fell off.

Held: That the plaintiff is entitled to recover the cost of replacing the pipeline but not that incurred by steps taken to anchor it securely to the bottom of the river by means of concrete weights.

2. That there is a discretion in a Court of Admiralty to award interest whether the rights dealt with arose *ex contractu* or *ex delicto* and such interest is not granted as something apart from the damages but as an integral part of them and the negligence exhibited by the master and officers of the defendant ship is so gross in its character to warrant the inclusion of interest as part of the damages to which the plaintiff is entitled.

ACTION by plaintiff to recover from defendants the cost of repairing a pipeline under the Detroit River alleged to have been damaged through negligence of the master and officers of defendant ship.

The action was tried before the Honourable Mr. Justice Wells, District Judge in Admiralty for the Ontario Admiralty District, at Toronto.

Peter Wright, Q.C. and *A. J. Stone* for plaintiff.

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F. O. Gerity, Q.C. and *R. Fraser* for defendants.

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

WELLS, D.J.A. now (July 26, 1962) delivered the following judgment:

This action arises out of a mishap to a pipeline under the waters of the Detroit River in the vicinity of the City of Windsor running from the plant of the plaintiff to a plant on the Michigan side of the river under the City of Detroit. Under an agreement which was proved before me the plaintiff undertook with another company, American Brine Inc., to service, repair and maintain the American portion of this pipeline and apparently the plaintiff was also either the owner or in possession of the various appurtenances belonging to the pipeline on both sides of the International boundary.

On the morning of December 12, 1958 the defendant ship was anchored in the Detroit River in the vicinity of the pipeline and on attempting to raise its anchor it became clear that one of the flukes of the anchor had in some fashion come in contact with the pipeline and had caught it. In the result by raising and lowering the anchor to free it from the pipeline the line was broken and fell to the river bed of the Detroit River, with the result that very heavy damages were suffered by the plaintiff.

The defendants' chief defence to this claim is that the defendant ship anchored where she did by reason of necessity owing to weather conditions and the visibility and it was necessary to use both bow and stern anchors owing to a heavy down current and ice conditions. The defendants admit that the anchor of the *Scott Misener* fouled a portion of the pipeline cable in the vicinity of the place of anchorage but says that this fouling was without negligence on its part. The plaintiff pleads negligence, trespass and nuisance and in the result claims very heavy damages.

In the pleadings it is not entirely clear whether the defendant ship was anchored within the territorial waters of Canada or those of the United States at the time the damage to the pipeline occurred. In paragraph 5 of the statement of defence it is pleaded the plaintiff had no title, right or license of occupation so as to maintain an action

in trespass. The problems raised by this defence are in my opinion, amply answered by the decision of the Court of Appeal in the case of *The Tolton*[1].

The pipeline in question was built under authorization from the American and Canadian Governments after, in the United States at least, public notice had been given of the intention to construct it. The permits covered two pipelines and what is called a recording cable. These were to be buried ten feet below the existing river bed. The purpose of the pipeline was to transmit saline solution or brine from certain salt mines on the Canadian side of the river.

It would appear from the evidence of one Wakefield, who had charge of the construction of this pipeline, that it was laid according to the requirements I have mentioned. He appears to have been a man of great practical experience and according to his evidence, the job was completed according to the permits with a minimum ten foot covering. I have no reason to doubt that evidence. According to his opinion, at the time the line was pulled up out of the water by the fluke of the anchor of the *Scott Misener* the ten foot coverage of silt had not had time to solidify and from the evidence at large the probability would appear to be that because of this the anchor might very well have penetrated down to where the pipeline actually was and became entangled with the pipe itself.

The plaintiff in presenting its case, filed a number of notices which were issued by the marine authorities in both Canada and the United States as to the position of this pipeline. In so far as the Canadian information to mariners was concerned, Mr. Barrick was called and stated that he was the District Marine Agent of the Department of Transport, living at Prescott, Ontario. The area of which he was in charge covered most of Southern Ontario from Beauharnois on the east to Sarnia on the west. He issued Exhibit 21 which was a notice to shipping numbered 125 and was issued on December 19, 1957 which advised that floating equipment was working in the district between the Canadian Brine Co. plant, Ojibway and the Solway Plant on Zug Island laying a pipeline. Masters were requested to reduce speed and exercise caution. He stated that this notice, and a number of others of the same kind, an example of which from United States may be found in Exhibits 17

[1] [1946] P. 135.

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and 20, were mimeographed and distributed by mail to all the principal steamship companies. There was no evidence produced which would show that this information in these notices if it was received by the owners of the *Scott Misener,* was ever communicated to the Captain or Third Mate who testified on behalf of the defendants. There was evidence, however, that it in all probability reached the owners of the *Scott Misener* and whether it was distributed or not I cannot say. If it was received by the owners there was a duty on the owners to communicate it to the officers and Masters of the ships that were navigating past the point where this pipeline was laid. Failure to disclose the existence of such a hazard as the pipeline in my view places a very heavy burden on the ship owners. The extent of that burden may be gauged and measured by the reasons of the House of Lords in the case of *The Norman*[1] to which I was referred.

Captain Rafuse, who was in charge of the *Scott Misener* at the time of this mishap, testified that he knew nothing about the pipeline until afterwards. In the year 1958 he had made some 41 trips up and down the Detroit River in the *Scott Misener* but despite two very large and legible signs, one on the American side of the river and one on the Canadian side, he apparently was not aware of the location of the pipeline in question nor did he know anything about it. This I do not believe. On the night that he anchored, visibility was apparently bad; it was hazy, some mist, and snow at dark. Nevertheless, it would appear from the evidence that both these signs were lighted and I can only conclude from Captain Rafuse's evidence that he anchored his ship without any care or regard to any signs which might be available to him which would indicate that he was anchoring in an area where he might do serious damage. His point of view apparently was that he had to clear the mouth of the Rouge River which runs into the Detroit River on the American side and that nothing else mattered. I am not at all satisfied that he had to anchor where he did or that the hazards of proper navigation made it necessary. Nor am I satisfied that he had not heard of the pipeline. His evidence was that at the time of this accident it was the third mate's responsibility to check the notices to mariners and indicate any changes shown by them on the chart. Exhibit 9 which is Chart 41 of the United States Lake Survey Edition of

[1] [1960] 1 Lloyds Rep. 7.

August, 1956, was a chart which was in the pilot house of the *Scott Misener* at the time that these events occurred. On it there is a very accurate line indicating the position of the pipeline drawn from the Detroit plant of the Canadian Salt Company with the word "pipeline" identifying it. Rafuse's evidence was that this was made the day after the accident after his ship got clear of the river and well into Lake Erie. He further stated it was made during one of the third mate's watches on December 12. I am very frank to say that I have very great doubt as to the truthfulness of the evidence of Rafuse in this matter. There is a strong probability that the marking of the chart indicating the pipeline in question, had been made at some time prior to the events with which we are concerned in this action. In cross-examination he was very unsatisfactory. He was asked if he had received the notices to the mariners in 1957 and 1958. He said that he might have missed some. He was shown a number of these notices and he said he might have seen them but could not recall them. I can only assume from the course which his answers took, that he was really indifferent to information such as that concerning the pipeline and at the time that he anchored he did so regardless of its location not from pure necessity but from indifference to anyone else's rights in the area in which he was anchoring. He was only concerned in my opinion, with his own convenience. At the time the actual accident occurred he was apparently advised over the public address system of the ship by the third mate who was supervising the raising of the stern anchor, that it had pulled up a cable. In point of fact it is quite clear from Holliday's and other evidence that what the anchor had pulled up was a portion of the pipeline. That should have been perfectly obvious to the mate. His instructions were to drop the anchor and pull it up again and see if the so-called cable would fall off. On cross-examination he was asked about this evidence and he again became rather vague and said he could not recall exactly what the third mate told him. He then said he thought he used the term "cable" but shortly after the accident after the ship according to his story, had got out to Lake Erie, he or the third mate wrote the word "pipeline" to indicate the position of the line and where it had occurred. Even accepting this somewhat sorry explanation, which I do not, the presence of the word "pipeline" on the

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chart is very eloquent in explaining what both Captain Rafuse and Glover, the third mate, thought their anchor had fouled.

One James Holliday was called on behalf of the plaintiff. He was the foreman for the salt company in their Windsor yard and the wells foreman in Windsor. He related how earlier in the morning of the 12th he saw the *Scott Misener* anchored off the power house of the plant and at that time he said no other vessels were in the vicinity; he related how earlier in the morning he had gone to the power house to relieve the man on duty and somewhere between 10.00 and 10.15 he heard a loud bang or clang. Shortly afterwards there was a second one and he went down to the basement where the various instruments governing the flow in the pipelines were situate and while he was there there was a third bang or clang and the recording meter measuring the flow to Detroit suddenly showed a large increased flow. He also related how when he first came on duty around 7.30 a.m. he had checked the signs on the Canadian side and even as late as 8.30 a.m. the lights were still on. The *Scott Misener* was at this time according to his estimate, approximately in the centre of the river.

Another employee of the plaintiff company, one Garvey, was called and he related having seen the *Scott Misener* anchored in the river and he could see the anchor chain but at the time he was looking, no anchor. He apparently was quite convinced at the time that the stern anchor of the ship had caught the pipe line. He also places the time of the mishap at around 10.15 and he later described the *Scott Misener's* actions in sailing away.

Another employee of the plaintiff company, one Gwilt, was also called. He apparently thought there was good visibility by 10 o'clock that morning and he also saw the stern anchor of the *Scott Misener* being pulled up and lowered. The evidence of these men coincided in part with that of captain Rafuse in that they saw the *Scott Misener* anchored in the river. They saw the stern anchor of the ship pulled up and down a number of times just prior to the time that the pipeline was broken. Some of them saw the *Scott Misener* sail down the river. They all appeared to agree that the accident happened somewhere between 10 to 10.15 a.m. It is I think, very significant as I have already said, that the witness Gwilt remembered that there was

good visibility as far as the other shore of the river from the Canadian side. There were, of course, two large signs—one on the American side of the river and one on the Canadian side warning of the presence of the pipeline and the danger attached thereto. About the time the *Scott Misener* was prepared to ship its stern anchor all the officers had to do was look out and they would have seen the signs which they admitted seeing a few minutes later. If these signs were not as seen by the Captain and the third mate of the *Scott Misener* and if at that time they did not realize the dangerous location in which they had chosen to anchor, in my opinion there was very little excuse for not doing so and they should have realized it. Once the fluke of the anchor broke the water with either the pipeline or cable attached to it, it should have been more than ever apparent that they were in trouble and to me it seems negligence amounting to almost complete recklessness to have directed the anchor be pulled up and down until the obstruction disappeared. For that action the Commanding Officers of the *Scott Misener* must take full responsibility.

Glover, the third mate of the *Scott Misener* also testified to considerable fog on the night before the accident but said that from 8 a.m. on, the river was safe to navigate. He was directly in charge of the hoisting of the stern anchor. He also said that one fluke was caught in a cable. He apparently advised the Captain and was told to lower the anchor to see if what was on it would come off. He apparently pulled it up and lowered it three times before it came up clear. According to his evidence he did not notice the sign about the pipeline until after this. Again, I very much doubt the truth of the evidence. In my view, no reliance should be placed on the evidence of either Rafuse or Glover.

To recapitulate:— In my opinion, from 8 o'clock on the morning of 12th December only, the notices indicating the position of the pipeline were clearly in full view of the officers of the *Scott Misener*. If they had not realized it earlier because of the weather conditions the night before at that time they should have realized it then. If they had not known of the approximate location of the pipeline it was because they paid no attention to their instructions in that respect and if the instructions in regard to the position of the pipeline were not passed on to them by the

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owners of the *Scott Misener,* that in my opinion does not relieve the shipping company because there was clearly a duty on it to transmit information as to the hazard of the pipeline being present at the bottom of the river. Finally, when the fluke of the anchor did bring the pipeline up it should have been perfectly apparent to everyone that they were not dealing with a cable but also with a part of the pipeline. Despite that, the Master of the *Scott Misener* directed that the anchor be raised and lowered until the obstruction fell off and in doing so he undoubtedly fractured the pipeline. This action of his I can only characterize as the reckless disregard of the rights of other users of the river amounting, in my opinion, to negligence of a very gross character.

In discussing his actions, reference may be made to the judgment of Earle C.J. in the old case of *Telegraph Company v. Dickson*[1]. While he was dealing with the subject of pleadings his observations in the reasons he gave are very pertinent to the issues with which I am dealing. Captain Rafuse's action in then sailing off I can only characterize as evidence of a reckless disregard of the rights of others.

Under the circumstances the plaintiff should succeed. The plaintiff's testimony is that the balance which it should receive for the replace of the pipeline is $386,472.06. When the pipeline was replaced, steps were taken to anchor it securely to the bottom of the river by means of concrete weights and quite obviously what money that the plaintiff chose to spend in this way by way of replacement is not chargeable to the defendants and is not the direct result of the negligence of the Captain and other officers of the *Scott Misener*. The plaintiff should have judgment for this sum.

In argument, counsel for the plaintiff also argued that they were entitled to interest on the cost of replacement of the pipeline limited as I have indicated. Counsel for the defendants argued that in Admiralty cases interest has not been allowed save in collision cases and then only as an allowance forming part of the damages for loss of use. The authorities, however, do not appear to confirm this submission. In the Exchequer Court of Canada in the case of *The Ship Pacifico v. Winslow Marine Ry. and Shipbuilding Co.*[1], Maclean J. dealt with repairs done to a foreign vessel in a

[1] 15 Common Bench Reports 758 at 775, 777.
[2] [1925] Ex. C.R. 32 at 35.

foreign port and where in the circumstances of the case there was a contract to do certain repairs to a vessel and an agreement to pay within thirty days from completion, the Court in giving judgment in the exercise of its equitable jurisdiction allowed interest on such amount from the date when the payment thereof should have been made as agreed. At p. 36 Maclean J. said:

On March 22, the plaintiff rendered an account to the *Pacifico* and owners for the materials supplied and the work performed, in the sum of $12,346.43, upon which the defendant paid on account, the sum of $7,500, on May 15, 1923, leaving a balance of $4,846.43. In the formal judgment the learned trial judge allowed interest at the rate of 5 per cent from April 5, 1923, such date being approximately thirty days subsequent to the completion of the work. The written reasons for judgment of the learned trial judge, is devoted entirely to the question as to whether the plaintiff was entitled to interest, and he there discusses the question quite exhaustively.

The defendant's counsel contended that the rule in force here as to interest, is the same as in England, and that there the rule of the Admiralty Court, since under the Judicature Act it became a division of the High Court of Justice, is the same as in the High Court of Justice, and that there it was not the practice prior to the Judicature Act or since, and both before and since the passing of the statute, 3-4 Wm. 4th, c. 42, to allow interest in cases similar to the one under consideration. He referred to *London, Chatham and Dover Railway v. South Eastern Railway* [1893] 63 L.J. Ch. 93; [1893] A.C. 429, as conclusive of the matter, though I understood him to admit that if this cause had been tried before the Judicature Act, and before the transfer of the Admiralty jurisdiction to the High Court of Justice, that the doctrine of the Admiralty Court as to interest might be applied in this case.

I cannot find any authority for the submission that the Judicature Act has changed the jurisprudence long established by the Court of Admiralty. The Judicature Acts of 1873 and 1875 amalgamated the English Courts and transferred to the High Court of Justice all the jurisdiction which had been exercised by the different courts, so that every judge of the High Court exercises every kind of jurisdiction possessed by that court, but these changes neither conferred new Admiralty jurisdiction, nor did it take away from that jurisdiction. It does not appear to me that the Judicature Act by intendment or otherwise, changed the substantive law as administered in Admiralty Courts, and in no way affected the powers of such courts, and that they retain all the powers they had before that Act. The point in controversy is one of substantive law I think, and not of practice or rule.

This was a case in admiralty where the right to damages arose *ex contractu*. Discussing the matter generally reference may also be made to the decision in the case of *The Joannis Vatis* (No. 2)[1]. The President Sir Henry Duke, in giving judgment made these observations at pp. 223, 224:

I next proceed to determine what sums are due and unpaid under the plaintiffs' judgment and what process of execution is available to the plaintiffs. The claim of the plaintiffs for interest on their judgment debt, as it

[1] [1922] P. 213.

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was pressed, is for 5 per cent. On £100,000 since the date of the judgment in the Court of Apepal, which date it bears. Under the ordinary practice of the High Court a judgment debt carries interest from its date at 4 per cent. (1 & 2 Vict. c. 110, s. 17; R.S.C., Order XLII., r. 16). That the plaintiffs' damages had to be assessed before the judgment could be completed by the Court's confirmation of the assessment might—but I do not pause to determine whether it would—have been immaterial in an action in the King's Bench Division. Here two special matters are to be considered. In this jurisdiction a rule exists with regard to interest upon damages which is well established and proper to be taken into account. The registrar and merchants include in their computation of damage by collision interest upon the items of claim from the time of accrual of the damage until the date of the assessment. The practice was discussed and confirmed in *The Kong Magnus* [1891] P. 223, and is in conformity with what was said long since by Lord Stowell in *The Dundee* (1827) 2 Hagg. Adm. 137, 143. The sum so calculated is given not as interest on a debt but as part of the damages. During recent years interest as damages has been reckoned in this way at 5 per cent., which perhaps explains the plaintiffs' demand of a 5 per cent. rate in their claim. Not only is this practice material for consideration as to the date from which interest can be held to run. It is necessary to remember also that—as the plaintiffs concede—the damages payable by the defendants are limited to £100,000. Interest upon items of damage down to the assessment of the loss would have been recovered out of this amount if the total claims had not exceeded £100,000. Really the claim is for damages. There was no allegation of default of payment by the defendants of the £100,000 after that sum had been found to be due, and I have come to the conclusion that the only time in respect of which interest can properly be awarded is the period between the judgment of the Court of Appeal, February 17, 1919, and the judgment of the House of Lords, December 19, 1919. The defendants, by their appeal to the House of Lords, postponed the settlement of the claims of the plaintiffs by 309 days, and they must pay interest on £100,000 at 4 per cent. for that time.

The matter has been more recently discussed in the case of *The Berwickshire*[1]. It is true that this is a case of a collision. The judgment is summarized in the headnote in the following words:

Held, that, as the true principle underlying the award of interest in Admiralty was that, in every pound's worth of damage in respect of which interest was ultimately awarded, the interest accrued potentially from the moment when the damage was suffered until the liability was adjudged and the amount finally ascertained, the plaintiffs were entitled to interest from the date of the collision until the date of the registrar's award.

Lord Merriman in giving judgment at p. 208 said:

As I have already indicated, there can be no doubt that the principle of including in the damages for a collision, at the discretion of the judge, interest on the amount recovered, at a rate, for a period, and whether in respect of the whole or part of the amount recovered, all of which matters are also respectively at the discretion of the judge, was firmly embodied in the Admiralty jurisdiction at a time when the right to award interest by way of damages at common law depended, speaking generally, on the

[1] [1950] P. 204

Statute 3 & 4, Wm. IV, c. 42, ss. 28 and 29, or on the express terms of a contract, or on those imported into mercantile contracts by the custom of merchants, as, for example, on bills of exchange or promissory notes; see the notes to the common indebitatus count for interest, in Bullen and Leake's Precedents of Pleadings (3rd ed.), pp. 51-52.

As to the Admiralty practice, it is unnecessary to multiply authorities. I need only refer to *The Hebe* (1847) 5 Notes of Cases 176, 182, *The Gazelle* (1844) 2 Wm. Rob. 279, 281, per Dr. Lushington in each case; *The Kong Magnus* [1891] P. 223, 226, per Sir Charles Butt; and *The Joannis Vatis* (No. 2) [1922] P. 213, 223, per Sir Henry Duke P. There is also a very clear statement of the principle by Sir Robert Phillimore in *The Northumbria* (1869) L.R. 3 A. & E. 6, 10.

Distinguishing the authorities cited in support of the proposition that the right to award damages depended solely on the Statute 3 & 4 Wm. IV, c. 42, and the proposition that the Admiralty practice was erroneous as being at variance with the common law both before and since the passing of the statute, Sir Robert Phillimore said (1869) L.R. 3 A. & E. 6, 10: "But it appears to me quite a sufficient answer to these authorities to say, that the Admiralty, in the exercise of an equitable jurisdiction, has proceeded upon another and a different principle from that on which the common law authorities appear to be founded. The principle adopted by the Admiralty Court has been that of the civil law, that interest was always due to the obligee when payment was not made, ex mora of the obligor; and that, whether the obligation arose ex contractu or ex delicto."

Discussing the period from which the interest is to be reckoned, Sir Robert Phillimore Ibid. 11, 12 pointed out that the court should be guided by the principle of restituto in integrum, and he referred to the argument that the statutes limiting liability had adversely affected the established principles of the court as follows Ibid. 12: "The question is, how are these principles affected by the statutes which limit the liability of the wrongdoer. In these statutes the legislature introduced a new principle, the object of which was to give some protection to the owner against the wrongdoing of his servant, the master of the vessel. They preserved the principle of restitutio in integrum in cases where, with his actual fault and privity, the damage had been inflicted on the sufferer; but with this exception, they limited his liability to a certain definite sum. In the latter case, therefore, this limited amount took the place of the restituto in integrum; but the principle still remains that the liability to this amount attaches from the time of the collision; and there seems no reason why interest should not accrue on the delay to pay that limited amount, as well as in the case where the amount is unlimited. Indeed, the equity of the thing is the other way, for to refuse this interest would be to diminish still further the natural right of the sufferer to full compensation for the injury which he has sustained. It is to be observed that the sufferer does not, where interest is awarded, obtain interest on the amount of his damage, but on the limited amount, or on his share of the limited amount to which the statute has restricted the liability of the wrongdoer. In the case of a vessel without cargo being sunk, it is clear that the interest would date from the time when the liability attached, that is, from the moment of the collision. Nor, when the case is examined, does it appear that a different rule ought to apply when the vessel carries cargo. Under the rule of restituto in integrum the cargo-carrying vessel did not obtain interest from the date of the collision, because she received it in the shape of freight at the port of delivery; but where the amount of the liability is limited, and

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the sufferer does not receive full compensation, the reason which fixes the date of the probable arrival at the port of delivery as the date from which interest shall run does not apply."

It would seem under the authorities of these cases to be clearly established that there is a discretion in a Court of Admiralty to award interest whether the rights being dealt with arose *ex contractu* or *ex delicto*. It is interesting to note that it was Sir Robert Phillimore's judgment in *The Northumbria* case which was relied on by Martin L.J.A. in delivering judgment at trial in the *Winslow Marine Railway and Ship Building Company v. The Ship Pacifico*[1] case, the judgment of which in appeal I have already quoted. The trial judgment was, of course, expressly approved by Maclean J. on appeal. Now in the case at bar it is quite true that no special claim for interest was expressed in the statement of claim but as I understand the equitable jurisdiction vested in the Court of Admiralty it is quite clear interest is not granted as something apart from the damages but as an integral part of them. It is quite clear that the jurisdiction of the Admiralty Court in Canada is as wide as that vested in the Admiralty Division of the High Court in England and indeed sec. 18 of *The Admiralty Act* being ch. 1, R.S.C. 1952 makes that quite clear. It sets the matter out as follows:

> 18. (1) The jurisdiction of the Court on its Admiralty side extends to and shall be exercised in respect of all navigable waters, tidal and non-tidal, whether naturally navigable or artificially made so, and although such waters are within the body of a county or other judicial district, and, generally, such jurisdiction shall, subject to the provisions of this Act, be over the like places, persons, matters and things as the Admiralty jurisdiction now possessed by the High Court of Justice in England, whether existing by virtue of any statute or otherwise, and be exercised by the Court in like manner and to as full an extent as by such High Court.

It therefore becomes a question of whether this is a case in which the exercise of my discretion as to interest should be allowed. In the view I have of the evidence as a whole, the negligence exhibited by the Master and officers of the defendant ship is so gross in its character to warrant in my opinion, the inclusion of interest as part of the damages to which the plaintiffs are entitled.

The plaintiffs, therefore, should have judgment for their damages including interest from December 12, 1958 at the usual rate, i.e. five pre cent. While there was considerable

[1] [1924] Ex. C.R. 90.

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evidence adduced at the trial as to the correctness of the figure claimed by the plaintiffs I would not go into any great detail as I deemed the more precise determination of the figure if it was objected to should be determined by way of reference. If the defendants are not satisfied to accept this amount that they then may at their own risk as to further costs, have reference to the Registrar of this Court to determine what the proper cost of the reconstruction of the pipeline properly chargeable to the defendants amounts to. Such intention should be indicated to the plaintiffs within thirty days from the date of this judgment, otherwise the plaintiffs are to have judgment for the sum claimed, interest and costs. If the defendants prefer to proceed with a reference the plaintiffs should have the costs of this action down to this judgment in any event and the costs of the reference I leave to the Registrar to whom the matter is referred.

Judgment accordingly.

1961

Nov. 21

1962

Sept. 11

BETWEEN:

DAVID MILLER .....APPELLANT;

AND

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

Revenue—Income—Income tax—Payment to real estate trader to relinquish option—Capital or revenue—The Income Tax Act, R.S.C. 1952, c. 148, ss. 2(3), 3, 4, 139(1)(e)—Civil Code, arts. 1476, 1477.

Appellant obtained from G an option to purchase certain farm land. The option stipulated *inter alia* that it must be accepted not later than May 28, 1956, and be accompanied by a deposit of $25,000. G died a few days later and the appellant on May 25, 1956, forwarded his acceptance in writing together with a certified cheque of $25,000 payable to G's estate. G's personal representatives refused to honour the option and after negotiation appellant surrendered his rights thereunder on payment of $50,000 and the return of his deposit. In re-assessing the appellant for the year 1956 the Minister added $50,000 to the appellant's declared income. An appeal from the assessment was dismissed by the Tax Appeal Board. On a further appeal to this court the taxpayer submitted that the sum in question was paid for the surrender of a right separate and distinct from the land and was neither profit or income but a capital sum. The Minister contended that payment for breaches of contract are capital receipts when received as compensation for loss of capital assets but are income from a business when received

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in lieu of profits from a business. That the appellant was a trader in real estate and had he acquired the optioned land it would have constituted stock in trade and therefore what he received was compensation for loss of inventory.

Held: That the appellant was engaged in the real estate business in the widest sense of the term.

2. That transactions commonly called "options" in the Province of Quebec are governed by the provisions of the *Civil Code* and that, as provided by article 1471, G's estate was legally entitled to revoke the option by returning appellant his deposit and paying him double that amount.

3. That the resulting gain was one which any regular dealer in real estate would experience in the ordinary course of his business and, as the appellant failed to prove the instant transaction occurred outside the ordinary course of such business, the $50,000 payment constituted taxable income in his hands.

APPEAL from the Tax Appeal Board.

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

J. H. Blumenstein, Q.C. for appellant.

Paul Boivin, Q.C. for respondent.

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

KEARNEY J. now (September 11, 1962) delivered the following judgment:

The present appeal is from a decision of the Tax Appeal Board dated the 6th of April 1961[1], whereby a tax reassessment made against the appellant by the respondent, which added, *inter alia,* $50,000 to the taxpayer's taxable income for the year 1956, was confirmed and his appeal therefrom dismissed with costs.

Counsel for the parties agreed that the record of proceedings before the Tax Appeal Board, consisting of Exhibits A-1, A-2 and A-3 and a corrected transcription of the evidence given before the said Board, should constitute the case before this Court.

The case arose because the appellant, who was allegedly in the real estate business in Montreal, on May 16, 1956 obtained an option from the late Félix Goyer to purchase certain farm lands in Côte St-Luc, consisting of lot 101 and part of lot 99 on the Official Plan and Book of Reference

[1] (1961) 26 Tax A.B.C. 243; 61 D.T.C. 224.

of the Parish of Montreal, measuring 1,213,987 square feet (approximately 28 acres), at a price of 55¢ a square foot, totalling $667,692.95.

The option contained the following stipulations.

It could not be registered against the property and it only became effective provided it was accepted by the appellant not later than May 28, 1956 and such acceptance was accompanied by a deposit of $25,000 subject to forfeiture if the appellant failed to pay the balance of price, to wit, $420,128.56, which became due in three months and the remaining $222,564.28 which was payable in two years. As security for the payment of the last-mentioned sum, a portion of the property located between the Côte St-Luc Road and the Railway was to be hypothecated in favour of Félix Goyer, and, until this amount had been liquidated, no subdivision could be made on such portion of the property (Ex. A-1).

A few days after having signed the document, Félix Goyer died, and, on May 25, 1956, the appellant accepted the option in writing and enclosed a certified cheque for $25,000, drawn on the Bank of Nova Scotia and payable to the estate of the late Félix Goyer (Ex. A-2). According to the appellant, who was the only witness heard, for reasons undisclosed the Goyer estate declined to honour the option, and, as a result of negotiations, the appellant surrendered his rights under it in consideration of the payment of $50,000 by the estate and the return of his deposit.

The question at issue is whether, as contended by the appellant, the receipt by the taxpayer of the aforesaid sum of $50,000 was of a capital nature and not a trading transaction or profit from a business subject to tax within the meaning of ss. 2(3), 3, 4 and 139(*e*) of the *Income Tax Act*.

In support of his objection to the reassessment in issue it was submitted, on behalf of the appellant, that his interest in real estate was for investment purposes and that he secured the option on the lands described therein for the purpose of constructing high rise apartment buildings thereon, which he intended to retain as an investment; that he did not trade in options and that the cancellation of the instant option was unforeseen and the payment received was fortuitous and outside the course of his business; that

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the option was a right different and distinct from ownership; and that the added reassessment of $50,000 was neither profit nor income and unfounded in fact and in law.

Apart from denying the appellant's allegations counsel submitted that the compensation was taxable as income received by the appellant in lieu of profits from a business and that had he acquired possession of the land under option it would have fallen into the category of stock-in-trade or inventory and therefore what he received was compensation for loss of inventory and was taxable accordingly.

Counsel for the appellant submitted with justification that an option or a promise of sale in respect of real estate only becomes the equivalent of sale when accompanied by tradition and possession: *Léo Perrault Ltée v. Blouin*[1]. He also recognized nevertheless that gain derived from option sources may constitute taxable profit or non-taxable capital increment, depending on the occupational activities of the taxpayer.

I think it is also true to say that our courts have usually held that gain resulting from an isolated transaction concerning a purchase or sale of real property by a non-trader therein constitutes a capital gain, but that the reverse is true where the taxpayer is an habitual trader in real estate, and the same reasoning, I think, is applicable in the present case. It follows that the outcome of this appeal may well depend on the answer to be given to two questions—Was the appellant really engaged in the real estate business and did dealing in options form part of such business? In respect of the first question, as appears by his 1956 income tax return, the appellant described himself as a commission salesman, and, in his evidence, he stated, "I am in investment realties" (Ex. A-2). The following is an extract from the notice of reassessment contained in the said exhibit:

ADJUSTMENTS TO DECLARED INCOME

Previous net income declared		$ 7,329.62
Add:		
Profits		
Lot 106 MTL.	$ 18,036.15	
Lot 101 & 99 MTL.	50,000.00	
St. Leonard Real. Commission	2,744.00	70,780.15
		$ 78,109.77

[1] [1959] R.J.Q., B.R. 764.

The reassessment shows that apart from the $50,000 in issue the Minister added thereto profits amounting to $18,036.15 and $2,744 in respect of two other real estate transactions. No exception was taken by the appellant to the addition of the above-mentioned amounts to his previously declared income. His acknowledgement that the two transactions were taxable is unmistakable proof that he was making profits on the sale of real estate.

Mr. Miller's testimony also discloses that, both prior and subsequent to the transactions in question, he had been dealing in various types of land, either alone, in partnership with others or through the incorporation of companies. He had bought and sold nearly every type of real estate. He had incorporated a company known as Westminster Gardens Limited and transferred to the company lands which he owned, built 700 homes thereon and sold them. According to the transcript (pp. 10-16), as early as 1951 he bought lots on Goyer Street in Montreal and sold them. His explanation for the transactions was that he was green in the trade at the time and disposed of the lots and bought a few apartment buildings with the proceeds. He stated that in 1955 he purchased lot No. 395 in St-Léonard de Port Maurice, sold it, and his reason for selling it in the same year was that "he could not develop it because there was no services there."

He made a similar acquisition and sale in respect of lot No. 63 in Pointe-Claire.

In the same year as he took the option on the instant property in Côte St-Luc he purchased a lot close by and sold it. His reason for doing so, he said, "was that the School Commission wanted to build a school, so rather than going through expropriation procedures and waste time, he decided to sell it (p. 19)."

Again in 1957, he sold part of lot 427 in St-Léonard de Port Maurice; lot 29 in Duvernay; lot 293 in St-Rémi; lots 429A and 430 in St-Léonard de Port Maurice, as well as a farm, No. 497 (p. 23).

In 1958, in the Côte St-Léonard area, the appellant purchased lot 100 and sold half of it in the same year because another group of people were interested in the lot. "So not to make bad feelings", he turned over to them half of it (p. 21).

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In 1958, he bought a property on Wellington Street in partnership with one Finestein and disposed of it at a loss; bought a farm in Rivière-des-Prairies, sold it at a profit, declared the profit as taxable in his income tax return and claimed the loss on the Wellington Street property as a deduction from income (p. 30).

It is quite true, as appears by his income tax return, that through the years, acting sometimes alone and sometimes with associates or through corporations in which he held an interest, he succeeded in acquiring and retaining as investments a considerable number of revenue-producing properties of various types from which his declared income amounted to some $7,000 in 1956 (Ex. A-2); but his trading operations constituted his main source of income. Looking at his dealings as a whole, the conclusion is inescapable that prior and subsequent to the option on the 28-acre farm in question the taxpayer habitually bought real estate of various kinds in diverse places and, afterwards, turned them to account in the most favourable way that circumstances permitted. I might add that the appellant also admitted, in his testimony, that at times he had recourse to the sale of some properties in order to realize the money to finance the acquisition of others. In connection with lot 101 and part of lot 99 the witness stated:

"We would probably have to develop and sell part of it, but we would have developed ourselves the apartment land for investment".

Although unnecessary for the purposes of this judgment, I consider it would be reasonable to assume that, since the optioned properties consisted of 28 acres of farm land, had the option been consummated, the taxpayer would have plied his trade by disposing of sufficient vacant land to make the financing and construction of an apartment building feasable.

As to the second question, transactions commonly called "options" in the Province of Quebec are governed by the provisions of the Civil Code under the title "OF SALE", where they are considered as a promise of sale—of which there are two kinds: simple and one accompanied by giving of earnest.

Article 1476 states:

A simple promise of sale is not equivalent to a sale, but the creditor may demand that the debtor shall execute a deed of sale in his favor according to the terms of the promise, and, in default of so doing, that

the judgment shall be equivalent to such deed and have all its legal effects; or he may recover damages according to the rules contained in the title "Of Obligations".

Article 1477 reads as follows:

If a promise of sale be accompanied by the giving of earnest, each of the contracting parties may recede from it; he who has given the earnest, by forfeiting it, and he who received it, by returning double the amount.

As appears from copy of the receipt A-3, signed by D. Miller, the payment of the $50,000 which he received represented double the amount of earnest given by him and, in my opinion, falls within the provisions of Art. 1477.

In argument, the $50,000 in issue was, I think, erroneously treated as if it were an amount which the taxpayer consented to accept as compensation for breach of contract. The action of Goyer Estate in making the payment it did was in no sense delictual; it was simply availing itself of its legal right to revoke the option on returning the deposit of the taxpayer and paying double the amount so deposited by the taxpayer. In my opinion, the appellant, instead of being faced with an unexpected breach of contract, obtained payment of a predetermined amount to which he was legally entitled. I consider that the transaction and the resulting gain must, on the evidence before me, be regarded as one which any regular dealer in real estate would experience in his ordinary course of business.

As mentioned earlier, the taxpayer declared that the Goyer option was the sole instance in which he dealt in options—but I do not think that this statement has been substantiated. Among the cases referred to at trial by the appellant was *No. 698 v. The Minister of National Revenue*[1], a decision in which it was held that money paid to obtain cancellation of an option was not income from a business but a capital gain and from which an appeal to this Court was then pending. Subsequently, the Minister's appeal therefrom was maintained (see *The Minister of National Revenue v. Bonaventure Investment Co. Ltd.*[2]). As appears by the judgment of Dumoulin J., Bonaventure Investment, which was engaged in the real estate business, offered to purchase from Messrs. Morris Schwartz, Harry

[1] (1960) 23 Tax A.B.C. 408; 60 D.T.C. 136.
[2] (1962) 62 D.T.C. 1083; 26 C.T.C. 160.

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Finestein and David Miller 50 lots in the Town of Dorval and agreed to give them an option or a simple promise of sale on a further 50 lots. The offer was accepted by the three associates and the sale of the first 50 lots was completed. Having apparently regretted giving the option, the three associates, following protracted discussions, paid Bonaventure Investment $7,500 to surrender its option rights and the Minister added this amount to the taxable income of the latter Company for the year 1956 and the learned trial judge confirmed the reassessment on the grounds that the $7,500 constituted income from a business. A glance at the appellant's balance sheet *re* Dorval Project (attached to his income tax return Ex. A-2) leaves no doubt that the present appellant and his two associates are the same persons referred to in the *Bonaventure* case. It is common knowledge that in the Province of Quebec the giving and taking of options in real estate transactions are by no means unusual occurrences, and, apart from reflecting generally on the appellant's credibility, the above evidence discloses that his option in the instant case was not to his own knowledge the unprecedented event which he claimed it to be.

For the foregoing reasons I find that the appellant was engaged in the real estate business in the widest sense of the term, that he has failed to prove that the instant transaction occurred outside the ordinary course of such business and that the $50,000 in issue constitutes taxable income in the appellant's hands.

In view of the above finding I consider it unnecessary to deal with any additional issues raised.

The present appeal will be dismissed with costs.

Judgment accordingly.

1962
Mar. 26
Sept. 20

BETWEEN:

HER MAJESTY THE QUEEN .....PLAINTIFF;

AND

CONTINENTAL AIR PHOTO LIMITED ..... DEFENDANT.

AND BETWEEN:

CONTINENTAL AIR PHOTO LIMITED ..... SUPPLIANT;

AND

HER MAJESTY THE QUEEN .....RESPONDENT.

Revenue—Excise—Sales tax—Exemption—Meaning of term "portrait photographers" under the Excise Tax Act and Old Age Security Act—Excise Tax Act, R.S.C. 1952, c. 100, ss. 30, 34(2), Schedule III, as amended by S. of C. 1960, c. 30—Old Age Security Act, R.S.C. 1952, c. 200 as amended by S. of C. 1959, c. 14.

The Crown brought action to recover sales tax and penalties from the defendant under the provisions of the *Excise Tax Act*, R.S.C. 1952, c. 100, as amended, and the *Old Age Security Act*, R.S.C. 1952, c. 200 as amended, on sales affected between December 1959 and April 1960. The defendant, a company carrying on business of photographing farms from the air and selling such photographs to the farm and home owners, claimed exemption under the provisions of s. 34(2) of the *Excise Tax Act* and Regulation 11 thereof, which regulation provides exemption from sales tax to portrait photographers who sell exclusively to the consumer or user.

By petition of right the above-named defendant brought action to recover from the Crown sales tax paid by it on such photographs made by it between May and December 1959. The two actions were tried together. The sole point at issue in both cases was as to whether the defendant was a "portrait photographer" within the meaning of the *Excise Tax Act*, regulation 11.

Held: That although one meaning of "portrait" (in English) is the representation of an object, the predominant meaning, and that attributed to it by usage of the trade, is that of a representation of a person, either of his face or his whole person.

2. That as there is no definition of the word "portrait" in the *Excise Tax Act* or the *Regulations*, and as it is not defined in any other acts in *pari materia*, it must be given the meaning ascribed to the word by persons familiar with the subject matter of the legislation.

3. That in construing the words "portrait photography" the court must apply the rule that an exemption provision in a statute must be given its strictest meaning in order to give the benefit to the narrowest group

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Noël J.

possible and on applying the rule the court concludes that the defendant company's operations do not fall within the exemption provided under the term "portrait photography".

INFORMATION by the Crown to recover sales tax and penalties

and

PETITION OF RIGHT to recover sales tax paid to Crown.

The actions were tried before the Honourable Mr. Justice Noël at Edmonton.

J. D. Lambert for plaintiff-respondent.

T. H. Miller and *Barry Vogel* for defendant-suppliant.

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

NOËL J. now (September 20, 1962) delivered the following judgment in The Queen v. Continental Air Photo Limited:

This is an information in which the plaintiff claims from the defendant payment of the sum of $2,479.22 for sales tax in respect of sales of aerial photographs in the period December 1, 1959 to and including the 31st day of March 1960, penalties for non-payment thereof and costs.

The defendant company carries on business in Canada and has its head office in the City of Edmonton, in the Province of Alberta. Its method of operation is to have its photographers fly down country roads in the Province of Alberta and take pictures of private homes and farm buildings from the air. In order to sell the pictures to the owners of the houses or farms, the photographers must get the house or farm from the best possible angle. They, therefore, have the pilot fly around three or four times and then direct him to go down in that particular position where they think the picture will be best after which they take the picture. The photographs are taken from an approximate distance of one thousand feet and from a height that varies between four hundred and six hundred feet.

The films are then developed and a negative of each is printed and turned over to a salesman who calls on the owners of the homes or farms and tries to sell them a picture of their property as a souvenir or for whatever use the

owners may have. These photographs are made available in various sizes and can be either black and white, or coloured, or painted pictures. Ninety per cent of the defendant company's sales in dollar volume are of coloured and painted pictures and ten per cent in black and white. However, in the number of pictures, the black and white would outnumber the coloured. In the event the customer indicates he is willing to purchase the picture and wants to have it done in colour, the salesman has to mark down all the colours of all the buildings, machinery and flowers, trees and lawn and everything that appears in the picture, by means of a numerical colour key chart, thus establishing how to complete the photograph in accordance with the wishes of the customer. The order is then forwarded to the defendant's office, in Edmonton, where the photographs are enlarged to the desired size, mounted on a masonite backing and turned over to a colourist. The latter is one of several employees of the defendant company, trained in the use of colours by the president of the defendant company and his wife, and familiar with the colour key. Some of these colourists work in their homes and some in the defendant's office. The evidence is to the effect that the work of a colourist is a difficult one and that out of twenty-five applicants for the job of colourist, one only usually turns out to be suitable. Once the colouring is completed, the photograph is sprayed with a clear varnish in order to protect the oil and the picture. In some instances the owner of the property desires changes to be made in the picture, such as removing objects or adding some and, in such cases, the defendant company complies with such requests and has a trained man for such retouching jobs.

In some instances, approximately one in four or five, the photographs contain people who are attracted by the noise of the plane and come out for a look and in one in ten or twelve, they contain livestock.

A consumption or sales tax of eight per cent on the sale price of all goods produced or manufactured in Canada is imposed by s. 30 of the *Excise Tax Act,* R.S.C. 1952, c. 100 and one of three per cent is imposed by s. 10 of the *Old Age Security Act,* R.S.C. 1952, c. 200 as amended by S. of C. 1959, c. 14.

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It is not disputed that if the defendant is liable therefore the amount now claimed for tax is the amount to be paid by the defendant.

Indeed the only point at issue is as to whether the work done by the defendant company comes under the classification of portrait photography or not. If it does, then the defendant company is exempt from payment of sales tax during the period under review. If it does not, it cannot benefit from the exemption provided by the regulations and it must pay the tax.

These regulations are established under authority of s. 34, s-s. 2 of the *Excise Tax Act*, R.S.C. 1952 c. 100.

Regulation 11 which applies in this case reads as follows:

11. *Small Manufacturers Exempt under Section 34, Subsection 2.*

* * *

The following manufacturers, when selling exclusively by retail, i.e., to consumer or user, are classified as small manufacturers and are not required to obtain sales tax licences,— . . . portrait photographers who sell exclusively to the consumer or user.

In the 1960 Statute of Canada, c. 30, Schedule (III) of the *Excise Tax Act* was amended and *inter alia*, the words "of individuals" were added to the words "portrait photographers".

The question for determination, therefore, is whether or not the operations of the defendant company fall within the description of portrait photography.

Mr. Henry Kreisel, Ph.D., professor of English and head of the English Department of the University of Alberta, after looking up the meanings and uses of the words "portrait, portray or portraiture" in a number of dictionaries, such as Webster International and the Great Oxford English, stated that the original meaning of the word "portrait" was simply a picture of an object; this meaning, however, is now more or less obsolete; the meanings now in standard use are a pictorial representation of a person, especially of the face; also a likeness; and then the dictionaries move on to the other meanings which are also given, i.e., a visible representation, an image, a copy, a similitude, and finally a lifelike or realistic representation. He stated that in the *Tamarack Review*, some time ago, he saw an article about Montreal and Toronto and the title was "Portrait of Two Cities". He admits that the word "portrait" is certainly at times used in this derivative sense.

The meaning of the word "portrait" was scrutinized in *The Duke of Leeds v. Lord Amherst*[1]. The Vice-Chancellor, Sir L. Shadwell had this to say at p. 179:

> Now, with respect to the word "portrait", a definition has been given in the course of the argument; and I have looked into the matter myself to see what is the origin of the word, and what meaning is ascribed to it not only in English but in French dictionaries; and it seems that, to a certain extent, it is used in a more enlarged sense in the English than it is in the French language.
>
> The first thing that I have to observe about it is that, in an edition of Richelet's Dictionary, which was printed in the year 1732, the author speaks of the word "portrait" as a French word, and explains the meaning of it in Latin, and then gives an interpretation of it in French. He says: "Portrait: *Imago, picta effiges. Ce mot se dit des hommes seulement*; et en parlant de peinture, c'est tout ce qui représente une personne d'après nature, avec des couleurs." In the French dictionary which has been lately published by Fleming & Tibbins, the explanation is this: "Portrait: Resemblance d'une personne;" and there it stops. The word is evidently taken from the Latin words *"pertrahere"* or *"pertractare"*, both of which words derive their force from being compounded, in part, of the preposition *per*, which, when used in composition, signifies doing an act completely, thoroughly, or with labour; as in our word "perfect", and the Latin word "perfectum".

Then at p. 180 he refers to a definition of "portrait" in the English dictionaries by Dr. Johnson: "A picture drawn after the life", that is, corresponding to the life and by Bailey, which in his opinion is a very good dictionary because it is not confined to words found merely in books of authority, but contains also words which are in common use; according to Bailey "portraits" (with painters) are pictures of men and women either heads or greater lengths, drawn from the life.

In the *Duke of Leeds* case, the question to determine was whether a picture of the Duke represented on horseback with a battle in the distance passed together with all the other portraits by the bequest, the testator having bequeathed the portrait of himself, his grandfather and grandmother and of the Duke of Shomberg. The Vice-Chancellor was of the opinion and so added that "the miniature representation of a battle, which is introduced in the background, in order to denote that the principal subject was a great warrior, does not detract from its character as a portrait".

[1] (1843) 60 English Reports 178.

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The meaning of "portrait" was also thoroughly examined in *Re Layard*[1]. By his will, the testator gave to his wife a house in Venice and in London, together with the contents of those houses "excepting my pictures and excepting certain presentation testimonials".

The will then proceeded as follows:

> As to all and singular my said pictures (except the portrait of my late uncle . . . .) as well those in Queen Anne-Street as those at Venice, ... and after the death of my wife I give and bequeath all my said pictures (except portraits) or such of my said pictures as the trustees and the director for the time being of the National Gallery may select unto the trustees of the National Gallery and their successors to be held by them for the use and enjoyment of the British public forever as part of the national collection. But the portraits of myself and all my family and other portraits (except the said portrait of my said uncle . . . .) . . . . I give and bequeath after the death of my said wife, free of legacy duty, to my nephew . . . . for his absolute use and benefit.

In this case, Astbury, J., at p. 18 states that:

> The plaintiff's witnesses have stated, and I think rightly, that a portrait means, or at all events includes, a picture painted from life, intended to be a real representation of the sitter; or, secondly, a replica of a such picture; or, thirdly, copy of it, as distinguished from a picture which, though painted from an individual, is intended to represent not so much the character and features of the sitter as some particular vice, virtue, or other characteristic or ideal that the painter desires to express.

Lord Cozens-Hardy in this case, at p. 23, states that he accepts the definition of Mr. William Roberts that a portrait means: "a picture which has been painted from the life as a likeness or presentment of the person or persons the subject of the picture" or a replica or a copy of such a picture.

In the above case, in view of the context of the will, the word "portrait" was held to have the narrow meaning of family portraits as distinct from old masters and pictures of great artistic merit, but the definitions of the word here are, however, of some assistance in our present query in determining what is the meaning of portrait photography. Indeed it would appear here that it deals mostly or preponderantly with persons or individuals.

The dictionaries give the following definitions of "portrait":

Larousse:

> Image d'une personne reproduite par la peinture, le dessin, la photographie, etc.: Hyacinthe Rigaud a laissé de remarquables portraits. Objet d'une ressemblance parfaite: enfant qui est le portrait de son père. Littér.

[1] (1916) 115 Law Times 15.

Description des traits ou d'un caractère, d'une époque, etc.: La Bruyère excelle dans les portraits. Portrait en pied, portrait qui représente la personne tout entière. Portrait parlant, portrait si expressif qu'il semble parler. Portrait de famille, celui qui représente un des aïeux de la famille. Pop. Figure: endommager le portrait d'un rival.

Nouveau Larousse Illustré:

Ressemblance de quelqu'un, obtenue par un procédé artistique ou industriel: Portrait à l'huile, au pastel, au crayon.

* * *

—Souvenir, profondément gravé, des traits d'une personne: Une mère garde toujours vivant le portrait de l'enfant qu'elle a perdu.

—Description des traits ou du caractère d'une personne: Les portraits de La Bruyère. Description quelconque: Un portrait tout à fait satisfaisant de l'esprit français. (Ste Beuve).

—Pop. Figure: Endommager le portrait d'un rival.

—Loc. div.: Portrait en pied, Portrait qui représente la personne tout entière. Portrait parlant, Portrait si ressemblant, si expressif, qu'il semble qu'on ait sous les yeux l'original prêt à parler. Portrait de famille, Celui qui représente un des aïeux de la famille.

Littré:

. . . Portrait en pied, portrait qui représente une personne entière. Portrait parlant, portrait si ressemblant qu'il semble parler. Portrait flatté, portrait qui atténue ce qu'il y a de mal dans le modèle. Portrait chargé, portrait qui exagère les défauts du modèle. . . . Représentation exacte d'un objet quelconque.

Quillet:

Image d'une personne faite à l'aide du dessin, de la peinture, de la photographie, etc. Portrait à l'huile.—Portraits de famille, portraits des aïeux.

—Portrait en pied, portrait qui représente une personne entière, debout ou assise.—Fig. C'est son portrait, tout son portrait, se dit, au physique et au moral, de toute personne qui ressemble beaucoup à une autre.

Par anal. Description, soit de l'extérieur ou du caractère d'une personne, soit d'une chose quelconque. Portraits littéraires.

Funk & Wagnalls:

1. A likeness of an individual, especially of the face, produced by an artist in oils, watercolor, etc., or by photography. 2. Hence, a vivid description *of something or someone having existence.*

* * *

Portraiture: 1. A representation of an object. 2. The act or art of portraying; especially, the art or practice of making portraits. 3. Portraits or pictures collectively.

Portray: To represent naturally and vividly, whether by drawing, painting, etc., or by verbal description or by acting; depict. See synonyms under IMITATE.

1. The act of portraying by any method of depiction or delineation; as, the portrayal of a character on the stage. 2. The making of a likeness of persons, places, or things; picturing. 3. A portrait.

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Shorter Oxford:

1. A figure drawn, painted, or carved upon a surface to represent some object; spec. (now almost always) a likeness of a person, esp. of the face, made from life by drawing, painting, photography, engraving, etc. A solid image, a statue—1638. fig. An image, representation, type; likeness, similitude 1577. A verbal picture; a graphic description 1596.

Portray:—1. To make a picture, image, or figure of. transf. To make (a picture, image, or figure); to draw, paint, or carve; to trace—1604. To paint or adorn (a surface) with a picture or figure 1667. To picture to oneself; to fancy. To represent (e.g. dramatically). esp. To represent in words, describe graphically, set forth, late.

Webster:

1. A picture of an object. 2. Specif., a pictorial representation of a person esp. of the face, painted, drawn, engraved, photographed, or the like; a likeness, esp. one painted from life. 3. A carved or molded figure; a statute; a sculpture. 4. Portraiture; esp., painting of persons from or as from life. 5. A visible representation or likeness; an image; a copy; a similitude; a picture (sense 4). "Where that sad portraict Of death and dolour lay, halfe dead". Spenser. 6. Lifelike or realistic representation; unidealized delineation, description, etc.; as, a painting that fails as a portrait; a fair portrait of an age.

Portray:—1. To represent by drawing, painting, engraving, etc.; to make a picture or image of; delineate; depict; as, to portray a king on horseback. Take a tile . . . and portray upon it the city. 2. To describe or depict in words; to describe vividly; also, to represent dramatically; to act. 3. To draw, paint, carve, etc. To adorn with or as with pictures. To image mentally; to imagine; picture. To form; frame; fashion.

From all this I have no hesitation in saying that although one of the meanings of "portrait" (in English) appears to be that of a representation of an object, the predominant meaning is that of a representation of a person either of his face or even of his whole person. Should I, in view of this, have any hesitancy in arriving at this finding, I could, and I believe that I should, turn towards the popular sense of the word "portrait" or even its meaning by usage in the trade.

Mr. Bertran C. Hollingshead, manager for twenty-two years of McDermid Studios Ltd., portrait and commercial photographers, commercial artists, photographers, one of the larger photography businesses in Edmonton, states that his interpretation of the word "portraits" in the advertisements to be found in the yellow pages of the Edmonton telephone directory, is that it would be the photographing of people, mainly faces, but that it could be full length.

His interpretation of the word "commercial photography" is the photographing of objects, of houses, of buildings, scenes . . ." but ordinary commercial photography, as he interprets it, is pictures taken of objects other than people. At p. 32 of the transcript he was asked:

> Q. If you were asked by someone to photograph a garden, their garden, what would—how would you classify that kind of photography?
>
> A. We would classify that as commercial photography.
>
> Q. If the people themselves wanted to be in the picture, in the garden, how would you classify that?
>
> A. This would depend on whether or not the people—if the people were the most predominant thing in the picture, then we might classify this as portraiture; that is, if the people were the most important thing, because then we would have very little but background in the garden, it would just be a background; but if we were taking in the garden, taking in the whole yard, with the people in the background, then we would class this as commercial photography.

The division into commercial and portrait photography is, according to this witness, recognized throughout the photography business.

Mr. Arnskov Neilsen, president of Continental Air Photo, the defendant, implicitly recognizes this when he admits that his company is not listed under the classification of "portrait photographers" because it only does aerial photography and does not do portrait photography. Indeed, at p. 24 of the transcript, he says:

> A. They would probably come expecting to get a picture taken of themselves, which we did not set up to do, or the children.

The evidence discloses also that when McDermid Studios Ltd. do aerial photography of industrial plants or areas under construction, they always send a commercial photographer.

The 1961-62 *Directory of Professional Photography,* produced as Exhibit B, contains a listing of members with this classification, the top one with a "P" opposite for portraiture (including studios, homes, passports, schools, groups, children) and then there is a different classification for commercial photography. According to Mr. Hollingshead, portraiture in the trade is associated with people posing, either full length or head and shoulders, with proper lighting to bring out certain features and perhaps hide certain features, or subdue them, and with the subject person's

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knowledge. He, however, admits that sometimes the word "portrait" can be used in connection with a pet, such as a dog or a horse, if there was a great deal of skill used in the lighting of the head.

In cross-examination, however, he finally admitted that what he has done is to arbitrarily divide the skill employed by the people who take the picture between "commercial", "portraiture" and "industrial". With respect to the question as to whether the distance at which the picture is taken is of any importance in determining the nature of the photography, he has this to say:

> It ceases to be a portrait when the distance between is such that the operator could not tell the person being photographed what he wanted him to do, how he wanted him to move, what action he wanted him to take.

If we revert to the case of the *Duke of Leeds v. Lord Amherst, (supra)*, I believe that we can safely say, as argued by counsel for the Crown, that if a "portrait" was a representation of any object, then there would have been no difficulty in that case nor any hesitancy in finding, although there was a battle in the background of the picture of the Duke on horseback, that the picture was a portrait.

There is no definition of the word "portrait" in the *Excise Act* or the *Regulations,* nor is it defined in any other Acts in *pari materia.* It is an ordinary word in everyday use and is therefore to be construed according to its popular sense.

In Craies on *Statute Law,* 4th edition, p. 151, reference is made to *Grenfell v. I.R.C.*[1] in which Pollock B. stated that if a statute contains language which is capable of being construed in a popular sense such "a statute is not to be construed according to the strict or technical meaning of the language contained in it, but is to be construed in its popular sense, meaning of course, by the words 'popular sense' that sense which people conversant with the subject matter with which the statute is dealing, would attribute to it."

In *Attorney-General v. Bailey*[2] it was held that the word "spirits being a word of known importance . . . is used in the *Excise Tax* in the sense in which it is ordinarily understood". In that case the Court said that in common

[1] (1876) 1 Ex. D. 242-248. [2] (1847) 1 Ex. 281.

parlance, the word "spirit" would be considered as comprehending a liquid like "sweet spirits of nitre" which is itself a known article of commerce not ordinarily passing under the name of "spirit".

As also stated by Craies on *Statute Law*, p. 152, the rule is that the particular words used by the legislature in the denomination of articles are to be understood according to the common commercial understanding of the terms used, and not in their scientific or technical sense.

There is some authority to the proposition that if there is a difference in meaning between the definition of the word in the dictionary and the usage by persons who are familiar with the subject matter of the legislation, or whether there is any doubt about which definition in the dictionary is to be preferred, then the meaning given to the word by the persons who are familiar with the subject matter of the legislation should be preferred. cf. *Unwin v. Hanson*[1] and *The King v. Planters Nut and Chocolate Co. Ltd.*[2].

Mr. Hollingshead who, as we have seen, has considerable experience in the photography business, stated that there is in the trade a definite and distinct usage for the words "portrait photography" and the words "commercial photography" and that persons in the photography business would not regard Continental Air Photo Ltd., the defendant, as portrait photographers. Regulation No. 11, quoted above, which establishes the exemption for portrait photographers, differentiates between portrait photographers, commercial photographers and industrial photographers, thus giving effect to the division adopted by the trade. Indeed, this Regulation gives two exemptions for photographers, one is for portrait photographers who sell exclusively to the consumers or users, and they are entirely exempt, and the other exemption is for commercial or industrial photographers or any manufacturer or commercial or industrial photographers and this exemption applies only if the sales do not exceed $3,000.

We are not dealing here with a tax charging section but with an exemption provision, and therefore, if there is any doubt as to which of the two possible conclusions should be preferred, the narrowest and strictest should be adopted in

[1] [1891] 2 Q.B. 115. [2] [1951] Ex. C.R. 126.

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order to give the benefit of exemption to the narrowest group, consistent with the meaning to be given to the words "portrait photography".

Authority for this can be found in *W. A. Sheaffer Pen Company of Canada Limited v. M.N.R.*[1]. In this case, Thorson P. says:

> While the appellant's submission appears attractive at first sight and merits consideration I am of the opinion that it is unsound and must be rejected. There are several reasons for this conclusion. While it is well established that all charges must be imposed by clear and unambiguous language and that a person is not to be subjected to tax unless the words of the taxing statute expressly impose it and he is caught by them; *vide Partingdon v. Attorney-General* (1869) 4 E & I App. 100 at 122 and *Tennant v. Smith* [1892] A.C. 150 at 154 and numerous decisions of this Court such as *Connell v. Minister of National Revenue* [1946] Ex. C.R. 562 at 566, *David Fasken Estate v. Minister of National Revenue* [1948] Ex. C.R. 580 at 588; it should be noted that in the present case there is no question of imposition of any charge. Here the appellant seeks the benefit of a right of deduction to which it would not be entitled except for section 5(*p*) the opening words of which refer to the exemptions and deductions to which what would otherwise be taxable income is subject. The manner in which an exempting provision in a taxing statute should be construed has been dealt with in a number of cases.

And he refers to *Wylie v. City of Montreal*[2]. Sir W. J. Ritchie, C.J. of the Supreme Court, at p. 386, where he said:

> I am quite willing to admit that the intention to exempt must be expressed in clear unambiguous language; that taxation is the rule and exemption the exception, and therefore to be strictly construed;

Attention was called to the change in Schedule (III) (Statutes of Canada 1960, c. 30) by the addition of the words "of individuals" and it was argued that the amendment shows that a change was intended to be made.

That this is not the case appears by s-ss. 2 and 3 of s. 121 of the *Interpretation Act*, R.S.C. 1927, c. 158:

> 2. The amendment of any Act shall not be deemed to be or to involve a declaration that the law under such Act was or was considered by Parliament to have been different from the law as it has become under such Act as so amended.
>
> 3. A repeal or amendment of any Act shall not be deemed to be or to involve any declaration whatsoever as to the previous state of the law.

I must conclude that the amendment to remove all possibility of ambiguity was, I think, merely declaratory of what was always the true intendment of the previous words.

[1] [1953] Ex. C.R. 251 at 254.

[2] (1885) 12 Can. S.C.R. 384 at 386.

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My finding must, therefore, be that the defendant company's operations do not fall within the exemption provided under the term "portrait photography".

In the result, the plaintiff is entitled to judgment against the defendant in the amount claimed for sales tax, namely $2,479.22; the sum of $28.69 for penalties for non-payment of the sales tax as prescribed by s-s. (4) of s. 48 of the *Excise Tax Act*, R.S.C. 1952, c. 100 as amended for the months of January, February, March and April, A.D. 1960, and in the amount of $16.53 for each month thereafter from and including the month of May, A.D. 1960 to and including the date of payment of the said sum of $2,479.22 and for costs to be taxed. The penalties provided in s. 48(4) are mandatory in the event of non-payment within the time provided for in s. 48(4) and there is no power in this Court to waive such penalties.

Judgment accordingly.

NOËL J. now (September 20, 1962) delivered the following judgment in Continental Air Photo Limited v. The Queen:

Continental Air Photo Ltd., the suppliant in this case, is a body corporate incorporated under the *Companies Act* of the Province of Alberta with head office in the City of Edmonton, Province of Alberta, where it carries on the business of photographing homes and farms from the air. Its method of operation is to have its photographers fly down country roads and take pictures. In order to sell the pictures to the owners of the homes or farms, the photographers must get the house or farm from the best possible angle. They, therefore, have the pilot fly around three or four times and they direct him to go down in that particular position where they think the picture will be best, afterwards, they take the picture. The photographs are taken from an approximate distance of one thousand feet and from a height that varies between four hundred and six hundred feet. The films are then developed and a negative is printed and turned over to a salesman who calls on the owners of the homes or farms and tries to sell them a picture of their property as a souvenir or for whatever uses the owners may

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have. These photographs are made available in various sizes and can be either black and white, or coloured or painted pictures. Ninety per cent of the suppliant company's sales in dollar volume are of coloured or painted pictures and ten per cent in black and white. However, in the number of pictures, the black and white would outnumber the coloured. In the event the customer indicates he is willing to purchase the picture and wants to have it done in colour, the salesman has to mark down all the colours of all the buildings, machinery and flowers, trees and lawn, and everything that appears in the picture, by means of a numerical colour chart, thus establishing how to complete the photograph in accordance with the wishes of the customer. The order is then forwarded to the suppliant's office, in Edmonton, where the photographs are enlarged to the desired size, mounted on a masonite backing and turned over to a colourist. The latter is one of several employees of the suppliant company, trained in the use of colour by the president of the company and his wife and familiar with the colour key. Some of these colourists work in their homes and some in the suppliant's office. The evidence is to the effect that the work of a colourist is a difficult one and that out of twenty-five applicants for the job of colourist, one only usually turns out to be suitable. Once the colouring is completed, the photograph is sprayed with a clear varnish in order to protect the oil and the picture. In some instances, the owner of the property desires changes to be made in the picture, such as removing objects or adding some and, in such cases, the suppliant company complies with such requests and has a trained man for such retouching jobs.

In some instances, approximately one in four or five, the photographs contain people who are attracted by the noise of the plane and come out for a look and in one in ten or twelve, they contain livestock.

During a period extending from June 30, 1958, to December 31, 1959, the suppliant company remitted to the Department of National Revenue, Excise Tax Division, the sum of $16,161.40 purportedly in payment of sales tax on the sales of aerial photographs. Section 5 of the petition sets out the gist of the action. It reads as follows:

5. Your Suppliant now states that the said sum of Sixteen Thousand One Hundred and Sixty-one Dollars and Forty Cents ($16,161.40) was remitted by it during the period June 30th, A.D. 1958 to December 31st,

A.D. 1959 under mistake of law or fact as it was during this entire period exempted from the payment of such taxes under the provisions of the Excise Tax Act, R.S.C. 1952, Chapter 100 as amended, specifically Section 34(2) of the said Excise Tax Act and the regulation of the said Excise Tax Act under Section 34(2) as contained in Department of National Revenue Excise Division circular E.T. 1, Section 2(3)(*a*) and (*b*).

At the trial the suppliant admitted that his reference in his pleadings to circular E.T. 1, s. 2(3)(*a*) and (*b*) was incorrect and that the proper reference was Regulation 11 entitled "Small Manufacturers Exempt under Section 34(2)".

To this the respondent replies that the suppliant "upon the sale and delivery of the said goods became indebted to Her Majesty in the amount of $16,161.40 under the provisions of the *Excise Tax Act,* R.S.C. 1952, c. 100, as amended, and under the provisions of the *Old Age Security Act,* R.S.C. 1952, c. 200, as amended, and paid to Her Majesty the said amount.

A consumption or sales tax of eight per cent on the sales price of all goods produced or manufactured in Canada is imposed by s. 30 of the *Excise Tax Act,* R.S.C. 1952, c. 100, and one of three per cent is imposed by s. 10 of the *Old Age Security Act,* R.S.C. 1952, c. 200, as amended by R.S.C. 1959, c. 14.

It is not disputed that if the suppliant is liable, therefore, the amount now claimed as a reimbursement or refund is the amount the suppliant had to pay. Indeed, the only point at issue is whether the work done by the suppliant company comes under the classification of portrait photography or not. If it does, then the suppliant is exempt from payment of sales tax during the period under review and is entitled to a refund. If it does not, it cannot benefit from the exemption provided by Regulation 11 and the payment as made must stand. For the reasons set out in a decision of this Court *ante* p. 461 under number 167487 involving the same parties but where Her Majesty the Queen is plaintiff and the suppliant company is the defendant, I arrive here also at the same decision and find that the suppliant company's operations do not fall within the classification of "portrait photography" and, therefore, it cannot benefit from the exemption provided under the Regulations for

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portrait photography and doth order and adjudge that Continental Air Photo Limited is not entitled to the relief sought by its petition, and that Her Majesty the Queen recover from the said Continental Air Photo Limited her costs to be taxed, if any.

Judgment accordingly.

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2. Bank of Canada Act, R.S.C. 1952, c. 13, s. 20. No. 3.
3. Bar Act, S. of Q. 1953-54, c. 59 as amended. No. 1.
4. Bar of the Province of Quebec, by-laws 66, 67. No. 1.
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9. Crown Liability Act, S. of C. 1952-53, c. 30, s. 3(1)(a). No. 2.
10. Crown not liable. No. 2.
11. Damages claimed for loss of letter due to failure of clerk to place in suppliant's post office box. No. 2.
12. Exchequer Court Act, R.S.C. 1952, c. 98, s. 36(1). No. 1.
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14. Issue determined by provisions of Post Office Act and not by those of Crown Liability Act. No. 2.
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19. Petition of Right. Nos. 2 & 3.
20. Post Office Act, R.S.C. 1952, c. 212, s. 40 and regulations. No. 2.
21. Recovery allowed on quantum meruit basis. No. 3.
22. Whether agreement binding. No. 1.
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Code of Quebec, arts. 990, 1732—Exchequer Court Act, R.S.C. 1952, c. 98, s. 36(1).

Suppliant, a Montreal advocate, was engaged as legal agent by the Department of Justice and supplied with a document entitled "Instructions to Agents" which specified that an agent in submitting his account was to certify that the services indicated therein truly showed their nature, the time occupied, and the fees claimed. It further provided that such account was taxable by the Deputy Minister of Justice whose taxation was not appealable. Acting on the Department's instructions suppliant laid complaints against and prosecuted two persons for offences under the *Excise Act*. The accused pleaded guilty in the Court of Sessions of the Peace and were each fined $1,000 and costs. On an appeal the fines were reduced to $500 each and costs. Subsequently suppliant laid similar charges against 122 others all of whom pleaded guilty and were each fined $1,000 and costs. Suppliant then submitted two accounts to the Department, one for $130 covering his fees for the first two convictions secured, and a second for $1,360, his fees for the subsequent convictions. The first account was taxed at the amount submitted and the second at $380. Suppliant by Petition of Right sought to secure from the respondent the difference between the amount of his bill and that paid him. He alleged that he had complied with the terms of the "Instructions to Agents" and that the fees claimed by him were in accordance with its provisions. In the alternative he alleged that the instructions were *ultra vires* and that his fees were governed by the provisions of the *Bar Act*, S. of Q. 1953-54, c. 59 as amended, and by-laws 66 and 67 of the Federal Council of the Quebec Bar. *Held:* That there was nothing in the provisions contained in the "Instructions to Agents" which if followed would lead the suppliant open to a charge of having committed an act derogatory to his profession. Although the profession of advocates is governed by the *Bar Act*, advocates as agents, are by virtue of art. 1732 of the *Civil Code* subject, insofar as they apply, to the general rules governing mandates, and it could not be argued that the contract of agency in question contravened art 990 of the *Code* which states that the consideration is unlawful when it is prohibited by law or is contrary to good morals or public order. 2. That the suppliant was bound by the contract of agency by which the Deputy Minister of Justice was given wide discretionary powers to determine the amount of his account and, in the absence of evidence to justify the conclusion that the taxing officer had acted in bad faith, or that the amount at which the account was taxed was unreasonable, there was no reason that the Court should interfere. 3. That although the "Instructions to Agents" specified the taxation was not appealable, s. 36(1) of the *Exchequer Court Act* vested jurisdiction in the Court to hear an appeal therefrom. BENOIT GONTHIER v. HER MAJESTY THE QUEEN.....21

2.—*Petition of Right—Crown Liability Act, S. of C. 1952-53, c. 30, s. 3(1)(a)—Post Office Act, R.S.C. 1952, c. 212, s. 40 and regulations—Damages claimed for loss of letter due to failure of clerk to place in suppliant's post office box—"Mishandling of anything deposited in a post office"—Issue determined by provisions of Post Office Act and not by those of Crown Liability Act—Crown not liable.* Suppliant brings his petition of right to recover from the Crown damages allegedly suffered by him due to the failure of a postal clerk in a post office known as Station H in Montreal, Quebec, to place in a box in that post office rented by suppliant a letter containing a cheque for $12,000 which had been mailed to him at that address from Caracas, Venezuela, as a result of which he was unable to complete arrangements for shipping a large number of prize cattle to Venezuela. Suppliant relies on s. (3), s.-s. (1), para. (*a*) of the *Crown Liability Act*, S. of C. 1952-53, c. 30. Respondent denies that suppliant suffered damages due to negligence of an employee and pleads s. 40 of the *Post Office Act*, R.S.C. 1952, c. 212 and the regulations made thereunder. *Held:* That the suppliant is not entitled to any of the relief claimed in the petition of right. 2. That s. 40 of the *Post Office Act* vests in the Crown the power or authority to determine by regulation to what extent, if any, it will be liable for claims arising from the loss, delay or mishandling of anything deposited in a post office, and that in the absence of anything to the contrary contained in the Act itself or its regulations no liability exists. 3. That the word "mishandling" in s. 40 of the *Post Office Act* means *inter alia* to handle badly, improperly or wrongly and accurately describes the error which was made in not placing the letter addressed to suppliant in the proper box in the post office. *Lever Brothers Co. Ltd. et al. v. The Queen*, [1960] Ex. C.R. 61; [1961] S.C.R. 189, distinguished. 4. That the issue raised in the case is to be determined by s. 40 of the *Post Office Act* and not s. 3(1)(*a*) of the *Crown Liability Act*. ADOLFO LENDOIRO v. HER MAJESTY THE QUEEN 58

3.—*Petition of Right—Claim against Crown for services rendered in connection with sale of securities—Bank of Canada Act, R.S.C. 1952, c. 13, s. 20—Financial Administration Act, R.S.C. 1952, c. 116, Part IV, ss. 39, 41, 42 and 43—Minister not competent to contract—Necessity of Order in Council—No liability on quasi contract—Recovery allowed on quantum meruit basis—Comptroller's certificate.* Suppliant brings its petition of right to recover from the Crown the sum of $60,000 for breach of an alleged contract in 1957. It claimed to have been requested

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in December, 1956 and in January, 1957 to prepare advertising material, arrange television programmes and generally advertise the government's 1957 campaign for sale of Canada Savings Bonds. It alleged that it had been engaged by the Bank of Canada to perform such services in a previous bond sales campaign and that such arrangement entitled it to consider it would act likewise for the 1957 sales campaign but that its contract was terminated by the Minister of Finance on July 10, 1957, after certain expenses had been incurred and considerable work done in preparation for the campaign. Respondent contends, *inter alia*, that there was no binding contract entered into between the suppliant and the Crown and that the suppliant had rendered the services in question in the hope of getting a contract. *Held:* That there was no binding contract between the suppliant and the Crown at the time of the alleged breach in July, 1957. 2. That by virtue of the *Financial Administration Act*, R.S.C. 1952, c. 116, neither the Minister nor any one acting on his instructions was authorized to enter into a contract on behalf of the Crown relating to the borrowing of money or the issue or sale of securities relating thereto without Parliamentary authority to borrow the money and an Order in Council authorizing the Minister to enter into such a contract. 3. That neither in December, 1956 nor in January, 1957 nor at any time subsequently up to July 10, 1957 when its services were dispensed with was there any such Order in Council authorizing the alleged contract. 4. That since the Crown subsequent to July 10, 1957 had adopted some of the results of the services rendered by the suppliant and used them in the campaign later authorized and conducted it was bound to compensate suppliant on a *quantum meruit* basis. 5. That s. 39 of the *Financial Administration Act* provides no defence to such a claim as herein presented since that provision applies only in respect of contracts and affords no answers to claims not founded on a contract. WALSH ADVERTISING CO. LTD. v. HER MAJESTY THE QUEEN.....115

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INCOME TAX ACT, R.S.C. 1952, c. 148, ss. 12(1)(a), AND 12(1)(b).
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INCOME TAX ACT, R.S.C. 1952, c. 148, ss. 12(1)(a), 14(2)(3), 85(e), 139(1)(w), 2(a) AND 125(1).
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3. Patent Act, R.S.C. 1952, c. 203, ss. 2(d), 35, 36, 41(1). No. 1.
4. Substance claim must be limited to that substance when produced by process for its preparation claimed and particularly described or an obvious chemical equivalent. No. 1.
5. To validate product claim process must be valid. No. 1.

PATENTS—*Infringement—Claims for substances prepared or produced by chemical process and intended for food or medicine—Substance claim must be limited to that substance when produced by process for its preparation claimed and particularly described or an obvious chemical equivalent—To validate product claim process claim must*

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be valid—The Patent Act, R.S.C. 1952, c. 203, ss. 2(d), 28(1), 35, 36, 41(1) and (2). The plaintiff sued for infringement of its patent for an invention entitled "process for the production of substituted morpholines" alleging that the defendant by selling phenmetrazine hydrochloride tablets had infringed claim 8 of the patent, a claim for "2-phenyl-3-methylmorpholine when prepared by the process of claim 1, 2 or 3 or an obvious chemical equivalent". (Phenmetrazine is the generic name for 2-phenyl-3-methylmorpholine.) The defendant admitted the sale but denied infringement and attacked the validity of claims 1, 2, 3, and 8. The specification describes in general terms certain processes for the production of a class of substituted morpholines large enough to include many billions of them but nowhere until claim 8 refers to 2-phenyl-3-methylmorpholine except by way of an example of the class. The defendant contended that the specification should be construed as disclosing but a single invention of processes for making the whole class of substances claimed and on the basis of this construction raised a number of objections to the patent. The plaintiff submitted that as a matter of construction the specification disclosed two inventions, one relating to the class of substituted morpholines, the other to the single substance 2-phenyl-3-methylmorpholine. *Held:* That to give meaning to the specification as a whole it must be read as disclosing two inventions, one relating to the class of substituted morpholines and the other relating to the single substance 2-phenyl-3-methylmorpholine included in claim 8. 2. That as claim 1 is a claim for a process for the making of the whole class of substances referred to in the specification and does not state the starting material from which 2-phenyl-3-methylmorpholine may be made, it does not state the essential feature of a process for making 2-phenyl-3-methylmorpholine, and it cannot be regarded as a claim of the kind required by s. 41(1) of the *Patent Act* as interpreted in the *Winthrop case*. The substance claim of claim 8 therefore is not limited, as it should be to comply with s. 41(1), to that substance when produced by a process for its preparation which is claimed and claim 8 is accordingly contrary to s. 41(1). 3. That under s. 41(1) of the *Patent Act* a claim for a new substance to which the subsection applies must be limited not only to that substance when prepared by methods or processes which have been claimed but also to that substance when prepared by the methods or processes which have been particularly described or their obvious chemical equivalents, and since the claim to 2-phenyl-3-methylmorpholine in claim 8 is not limited to that substance when prepared by the methods or processes which are particularly described or their obvious chemical equivalents. Claim 8 is broader than s. 41(1) permits and is

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accordingly invalid. 4. That in a patent to which s. 41(1) of the *Patent Act* applies, the process claim which must accompany a product claim for a new substance must itself be a valid claim. A claim to an exclusive property to which the inventor is not entitled and which is therefore not authorized by the statute will not serve the purpose. 5. That a claim for processes which produce products which are not useful in the patent sense lacks utility and is therefore invalid. On the evidence it is improbable that all or the majority or even a substantial number of the conceivable substances comprised within the class defined in claim 1 have the utility referred to in the specification, claim 1 is accordingly invalid and because it is invalid, claim 8 is invalid as well. 6. That for the purpose of obtaining the pharmacological results obtained by oral administration, phenmetrazine hydrochloride is an equivalent of phenmetrazine and if made by one of the processes mentioned in claim 8, its sale would constitute an infringement of claim 8. 7. That on the facts the process by which the allegedly offending material was made did not involve as one of its steps the process of claim 1 as applied to the production of 2-phenyl-3-methylmorpholine from a particular diethanolamine of the class but did involve a process which was an equivalent of the process of that claim when applied to the production of 2-phenyl-3-methylmorpholine from that diethanolamine. It was not however an obvious chemical equivalent of the process of claim 1 within the meaning of s. 41(1) of the *Patent Act* and the claim of infringement accordingly fails. *Re May & Baker Ltd. et al.* 65 R.P.C. 255; 66 R.P.C. 8; 67 R.P.C. 23; *Winthrop Chemical Co. Inc. v. Commissioner of Patents* [1948] S.C.R. 46; *Commissioner of Patents v. Ciba* [1959] S.C.R. 378 at 383; *McPhar Engineering Co. of Canada Ltd. v. Sharp Instruments Ltd.* 21 Fox P.C. 1 at 55, referred to. C. H. BOEHRINGER SOHN v. BELL-CRAIG LTD. 201

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REVENUE—*Income—Income tax—Betting—When winnings subject to income tax—The Income Tax Act, R.S.C. 1952, ss. 3, 4 and 127(1)(e).* The respondent, a hotel proprietor, in the years 1949 to 1953 inclusive, won substantial sums by betting on card games and sporting events. The

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Minister in reassessing the respondent added these sums to the taxpayer's declared income. The latter's appeal from the assessment was allowed by the Income Tax Appeal Board. On an appeal by the Minister to this Court *Held:* That to be taxable under the *Income Tax Act* a gambling gain must be derived from the carrying on of a "business" within the meaning of that term as defined by s. 127(1)(*e*) of that Act. 2. That as there was no evidence that the taxpayer, during the years in question in relation to his betting, had conducted an enterprise of a commercial character, or had organized these activities as to make them a business, calling or vocation, the appeal should be dismissed. *Down v. Compston* (1937) 21 T.C. 60, *Jones v. Federal Commissioner of Taxation* [1932] 2 A.T.D. 16 and *Lala Indra Sin, In re,* [1940] 8 I.T.R. 187 at 218, followed. *Partridge v. Mallandaine* (1886) 18 Q.B.D. 276, *Graham v. Green* (1925) 9 T.C. 309, referred to *M.N.R. v. Walker,* [1952] Ex. C.R. 1, distinguished. HARRY EDGAR MORDEN v. MINISTER OF NATIONAL REVENUE.....29

2.—*Income tax—Income Tax Act, S. of C. 1948, c. 42, s. 14(1) and the Income Tax Act, R.S.C. 1952, c. 148, s. 85B(1)(b)—Capital or income—Profit on real estate transaction—Assessment on a cash received basis.* Appellant with ample funds on hand in the form of negotiable securities, borrowed from his bank for the purpose of purchasing a lot in the City of Vancouver intending to build a small hotel on the land in order to set up his son in business. Shortly after the acquisition of the property he sold it at a profit. Respondent assessed the appellant for income tax on the profit resulting from this transaction and from that assessment appellant appealed to this Court contending that such profit is capital gain. Appellant also in partnership with another entered into an agreement with two wholesale grocers to erect a warehouse on property leased from the C.P.R. and rent to the wholesalers. This was done and the transaction provided a large profit to the appellant who appealed from an assessment for income tax on that profit and from the manner in which it was made. *Held:* That the profits realized by appellant from both deals are income and assessable for income tax and such assessment to be in accordance with the provisions of the law regulating taxation of income returns accepted on a cash received basis as set forth in s. 14(1) of the *Income Tax Act,* S. of C. 1948, c. 42 and s-s. (1), Para. (*b*) of s. 85B of the *Income Tax Act,* R.S.C. 1952, c. 148. DONALD C. BROWN v. MINISTER OF NATIONAL REVENUE..... 51

3.—*Income—Income Tax Act—Compensation award by War Claims Commission for World War II loss—Direction award bears simple interest—Whether sum referred to as "interest", capital or income—The Appropriation Act, No. 4, 1952, S. of C. 1952,*

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c. 55—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 6(b) and 139(1)(ag). The appellants in 1953 made application to the War Claims Commission for compensation for property owned by them in Czechoslovakia which was partially destroyed by the German Army in World War II. The Commission recommended payment out ot the War Claims Fund to each of the appellants and that such amounts should bear simple interest from January 1, 1946 at the rate of 3% per annum. On October 10, 1958 this recommendation was approved by the Treasury Board and on October 17, 1958 cheques were forwarded the appellants' counsel by the Department of Finance together with a letter stating that the cheques enclosed represented the payments recommended by the War Claims Commission together with interest to October 10, 1958. In assessing each of the appellants for the year 1958 the Minister added to the income reported by them the amount referred to as "interest" in the Commission's award. In an appeal from the assessments *Held:* That the payments take their nature not from the motives for making them, or from what they are called, but from what in substance they are. 2. That in the case of each appellant the amounts paid was a capital grant no part of which was "interest" or "received as interest" within the meaning of s. 6(*b*) of the *Income Tax Act. Glenboig Union Fireclay Co. Ltd. v. Commissioners of Inland Revenue,* [1921] S.C. 400; [1922] S.C. (H.L.) 112; (1922) 12 T.C. 427; *Commissioners of Inland Revenue v. Ballantine,* (1924) 8 T.C. 595; *Simpson v. Executors of Bonner Maurice,* (1929) 14 T.C. 580; 45 T.L.R. 581, referred to. *Riches v. Westminster Bank,* (1947) 28 T.C. 159 distinguished. ROSEMARY GERTRUDE HUSTON v. MINISTER OF NATIONAL REVENUE.. 69
FREDERICK B. WHITEHEAD v. MINISTER OF NATIONAL REVENUE..... 69
ELSE B. WHITEHEAD v. MINISTER OF NATIONAL REVENUE..... 69

4.—*Income Tax Act 1948, S. of C. 1948, c. 52, s. 125(a)—Income Tax Act, R.S.C. 1952, c. 148, s. 137(2)—Income or capital gain—Failure to discharge onus of establishing Minister's assessment is wrong—Appeal dismissed.* In 1924, Prescription Optical Co. Ltd. (a British Columbia company) was incorporated by a number of ophthalmologists in Vancouver, its business being that of filling prescriptions for eye glasses. In 1931, all its tangible assets and the right to use its name were transferred to Imperial Optical Co. Ltd. which thereafter carried out all the operational functions of Prescription Optical Co. Ltd. The latter company, on certain conditions, had the right to repurchase the tangible assets and, if it did so, Imperial Optical Co. Ltd. could no longer use the name of Prescription Optical Co. Ltd. Pursuant to an agreement then entered into with the individual doctor-shareholders, Imperial Optical Co. Ltd. thereafter paid

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the said shareholders a commission on all prescriptions referred to Prescription Optical Co. Ltd. by the shareholders. In 1936, the appellant was registered as the owner of one share in Prescription Optical Co. Ltd. and thereafter until March, 1946 received commissions on all prescriptions so referred by him and paid income tax thereon. In 1946, the *Medical Act* of British Columbia was amended and after April 11, 1946, it was illegal for any doctor in British Columbia to take or receive any such commissions. In 1947, it was arranged that all the outstanding shares of Prescription Optical Co. Ltd. (24 in all) should be transferred to Standard Optical Co. Ltd.—a subsidiary of Imperial Optical Co. Ltd. Subject to certain conditions and adjustments it was agreed that Standard Optical Co. Ltd. should pay $320,000, that amount to be apportioned between the twenty then practicing shareholders of Prescription Optical Co. Ltd. in proportion to their referral of prescriptions to Prescription Optical Co. Ltd. during the three previous years, and that the payments so allotted should be made in ten equal annual instalments. The sum of $29,172.52 was allotted to appellant and it is admitted that in each of the years 1949 to 1953 he received $2,917.25, which amounts were added to his declared income for each of those years. An appeal to the Tax Appeal Board was dismissed and appellant now appeals to this Court. On behalf of the appellant it is submitted that the said sums were not income, but rather instalments of the purchase price of a capital asset, namely, the one share in Prescription Optical Co. Ltd.; and that all the shares were worth at least $320,000. For the Minister, it is submitted that the annual payments were taxable income on the alleged ground (*inter alia*) that part of the consideration for the price of the shares was the appellant's agreement to encourage his patients thereafter to have their prescriptions filled by Prescription Optical Co. Ltd. The Court was not satisfied that all relevant, available facts and documents relating to the transfers of the shares were put in evidence, particularly an agreement and letter signed by the appellant which formed "part of the consideration for the purchase and sale" of the shares. Other matters were not satisfactorily explained, such as (a) the agreement that if the appellant should die or retire from practice before the ten annual payments had been completed, Standard Optical Co. Ltd. would "pay one year's instalment plus *pro rata* for the number of months practiced since our previous payment", all the remaining instalments being cancelled; (b) the fact that the estates of three deceased shareholders, and one doctor who was about to retire, received no part of the purchase price. *Held:* That the appellant had not discharged the onus which lies upon the taxpayer to establish that there is error in fact or in law in the assessments under appeal. 2. That the

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appeal must be dismissed. JOHN ARCHIBALD MCLEAN v. MINISTER OF NATIONAL REVENUE 81

5.—*Income tax—Income Tax Act 1948, S. of C. 1948, c. 52, ss. 11(1)(c), 12(1)(c), 42(6) and 124(12)—The Income Tax Act, R.S.C. 1952, c. 148, ss. 11(1)(c), 12(1)(c), 46(7) and 136(12)—Deductions—Interest on debentures—Validity of assessment—Defect in notice of assessment—Appeal allowed.* Respondent company, a dealer in auto parts, bought and sold them to the general public at a profit and also to companies it controlled. In October, 1946, it borrowed $1,060,000 at 4½% interest from a bank and in December of the same year purchased several companies dealing in auto parts at a cost of $988,029. In December 1947 it issued debentures amounting to $1,000,000 bearing 3¼% interest and sold them to its bank which applied most of the proceeds in reduction of the company's bank loan. Respondent claimed a deduction for the interest paid on these debentures which deduction was disallowed by the appellant on the ground that the proceeds were not used to earn income from a business or property under s. 11(1)(*c*) of the Act but were used to acquire property the income of which was exempt and that s. 12(1)(*c*) applied. An appeal to the Tax Appeal Board was allowed and from that decision the Minister appeals to this Court. The respondent contends that the proceeds from the debenture issue had no connection with the purchase of shares of subsidiaries because the shares had already been bought and paid for in the previous year. The Minister at the hearing of the appeal from the Tax Appeal Board introduced new evidence which showed that the debentures issued in April, 1947 had been antedated to August 1, 1946. A subsidiary point raised was that the notice of assessment bore the facsimile signature of a person who was no longer the Deputy Minister of National Revenue for Taxation at the time. *Held:* That the appeal must be allowed. 2. That the respondent and its officers treated the debentures in the same manner as if they had been issued in August, 1946, when no bank loan existed and the debenture issue was contemplated when the loan was effected. 3. That the proceeds of the debentures were not used for the purpose of earning income from a business or property within the meaning of s. 11(1)(*c*) of the Act, and respondent was not entitled to deduct the interest payable on the debentures. 4. That any defect that may have existed in the assessment notice was remedied by s. 42(6) now s. 42(7). MINISTER OF NATIONAL REVENUE v. UNITED AUTO PARTS LTD. 96

6.—*Income—Income tax—Payment for surrender of lease—Whether income or capital receipt—Income Tax Act, R.S.C. 1952, c. 148, ss. 3 and 4.* The appellant in 1948 leased his theatre from January 1, 1949,

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at a yearly rental of $5,400 under a lease that provided that the lessee should operate it as a moving picture theatre for not less that nine months in each year. By an agreement entered into in June, 1953 the term was extended for five years from January 1, 1954 at a rental of $5,800 per annum with an option to renew for a further five years at a yearly rental of $6,000. The lessee failed to operate the theatre for the stipulated nine months in 1955, and in June, 1956, a new agreement between the parties provided *inter alia* that notwithstanding anything contained in the 1953 lease, the lessee upon the payment of a monthly rental of $600 commencing July 1, 1956, and payable to the end of the term, should be free to close the theatre and would be discharged of all obligations under the lease and that the lessor for the remainder of the term could make such use of the theatre as he saw fit. On September 1, 1956, the lessor leased the theatre to another tenant at a rental of $3,000 per annum subject to an option to purhcase at any time during the term of the lease for $38,000. Four months later the tenant vacated the premises and in 1959 the appellant sold the property for $21,000. In re-assessing the appellant the Minister added to his declared income for the year 1956 the sum of $3,600 and the sum of $7,200 to his declared income for each of the years 1957 and 1958. The taxpayer's appeal from the assessment to the Tax Appeal Board was dismissed. On an appeal from the Board's decision *Held:* That the appellant failed to establish that the closing of the theatre for longer than permitted or that the cancellation of the lease (assuming it took place), caused the property to depreciate and the appellant to suffer a loss when he came to dispose of it. 2. That the thirty monthly instalments of $600 each paid the appellant should be regarded as rental received, or payments in lieu of rental, or in the nature of casual profit derived from a property, and constituted income rather than amounts received on capital account. *Minister of National Revenue v. Farb Investments Ltd.* [1958] Ex. C.R. 113 at 119 followed. *Van Den Bergh Ltd. v. Clark* [1935] A.C. 431 and *Sabine (H.M. Inspector of Taxes) v. Lookers Ltd.* (1958) 38 T.C. 120 distinguished. ISRAEL GRADER v. MINISTER OF NATIONAL REVENUE 106

7.—*Dominion Succession Duty Act, R.S.C. 1952, c. 89 and R.S.C. 1952, Supplement, c. 317, s. 3(1)(g)—"Succession"—Pension to widow not provided by deceased husband—Non-contributory annuity provided by employer of deceased husband—Voluntary and benevolent undertaking on part of employer in recognition of past services—Capitalized value of annuity added to succession by Minister—Appeal from assessment allowed—Date of acquiring vested interest in the annuity—Calculation of value of interest—*

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Civil Code, Article 1029—"Accruing or arising by survivorship or otherwise on the death of the deceased". The abovenamed deceased, John Bassett, who died on February 12, 1958, was at the time of his death and had been for many years prior thereto a director and officer of the Gazette Publishing Co. Ltd. of Montreal, Quebec. On March 27, 1947 the company entered into an agreement which recited that Mr. Bassett had served the company in diverse capacities and offices throughout many years but that he was not entitled to any benefit under any existing pension plan of the company and that the company desired to enter into an agreement not only with regard to his continuing remuneration, so long as he should be president of the company but also appropriately recognizing his long and effective service in the company's interest. It provided for the payment of a pension to him for his lifetime on his ceasing to be the company's president and that after his death it would pay to his wife during her lifetime if she survived him a pension at the rate of $5,000 per year and that the benefits so provided were in recognition of the valuable services rendered by him to the company prior to the execution of the agreement. The capitalized value of the annuity to the widow was added by the Minister of National Revenue to the assets of the succession of the deceased and taxed accordingly. From that assessment the executors of the will of Mr. Bassett appeals to this Court. *Held:* That the annuity was not provided by the deceased but was of a non-contributory nature and constituted a benevolent undertaking on the part of the company for the deceased's past services which had been fully paid for and acquitted and could not form the basis for any further claim against the company by the deceased or his widow, and by accepting a guaranteed minimum salary from the company Mr. Bassett could not be said to be sacrificing his own interest in order to benefit his wife. 2. That the widow acquired a vested right in and to the annuity upon the execution of the agreement of March 27, 1947 providing for it even though contingent on her surviving her husband and it had an appreciable value in 1947 by reason of the difference in age of the husband and wife. 3. That the appeal must be allowed. ROYAL TRUST COMPANY *et al* v. MINISTER OF NATIONAL REVENUE.....147

8.—*Income tax—Partnership formed to sell beer—Profits used wholly for community—welfare—Whether tax exempt as a charitable or non-profit organization—Income Tax Act, R.S.C. 1952, c. 148 ss. 6(c), 15(1), 62(1)(e) and 62(1)(i)*. At a meeting of the leading citizens of the town of Mont-Joli it was decided that application be made to the Quebec Liquor Commission for the issue of a single licence for the sale of beer in the town and that the profit from such sale be used for social welfare, education and civic improvement. At the request of the meeting the respondent and two others agreed to supervise the distribution of the profits and following the issuance of a licence to him, the three entered into a partnership under the name of "Distributors Associated" whereby they renounced all claim to personal profits and proceeded to distribute the profits arising from the beer sales pursuant to the undertaking given the citizens' meeting. In assessing the respondent for the taxation year 1956 the Minister added to the respondent's declared income an amount deemed to have been his share of the partnership profits. The respondent's appeal from the assessment was allowed by the Tax Appeal Board and from that decision the Minister appealed to this Court. *Held:* That as it was established by the evidence that the respondent did not receive and had no legal right to claim any of the profits arising from the sale of beer, the provisions of ss. 6(*c*) and 15 of the *Income Tax Act* had no application. 2. That as the partnership was a charitable organization as defined by s. 62(1)(*e*) and a non-profit corporation as defined by s. 62(1)(*f*) of the Act, its income was exempt from taxation. MINISTER OF NATIONAL REVENUE v. CHARLES AUGUSTE BEGIN.....159

9.—*Income tax—Payment in settlement of claim for breach of option to convey lots to builder—Capital or income receipt—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4 and 139(1)(e)*. The respondent, whose business was the building of houses for sale, purchased fifty building lots from a syndicate and secured an option to purchase fifty more lots at the same price. The vendor subsequently refused to honour the option but on threat of suit paid the respondent $7,500 in settlement of its claim. In re-assessing the respondent for its 1956 taxation year the Minister added $7,500 to its taxable income. The respondent appealed from the assessment on the ground that the payment constituted non-taxable compensation for damages of a capital nature which should not have been treated as income. The Tax Appeal Board allowed the appeal. On an appeal by the Minister from the decision of the Board. *Held:* That the building lots in question formed part of the respondent's stock in trade and the payment of $7,500 was to compensate it for the loss of business profits and therefore was properly included in computing its taxable income. *Burmah Steam Ship Co. Ltd. v. Commissioners of Inland Revenue* 16 T.C. 67 at 71, and *Jesse Robinson & Sons v. Commissioners of Inland Revenue* 12 R.T.C. 1241 at 1247, referred to. MINISTER OF NATIONAL REVENUE v. BONAVENTURE INVESTMENT CO. LTD.....169

10.—*Income—Income tax—Compensation received by agent for loss of agency—Capital receipt or income.* The appellant company was incorporated in 1930 to carry on the

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business of a manufacturer's agent and wholesale merchant dealing in china and related wares. From its inception the appellant represented the manufacturers of the Royal Albert line of tea ware and in 1933 became sole agent in Canada for the sale of dinner, tea and toilet ware and ornamental and other goods manufactured by Doulton & Co. Ltd. The two agencies were the principal ones which the appellant operated and accounted for 80% of its business. As exclusive agent for Doulton & Co. Ltd., the appellant was remunerated by a commission on all sales in Canada whether the order was secured by it or placed directly by the customer. The Doulton products sold by the appellant consisted principally of dinnerware and figurines and there was no competition between these lines of goods and the other lines the appellant sold. The agency agreement between the appellant and Doulton & Co. Ltd., provided that it should remain in force for one year from March 31, 1933, and it was determinable upon three months notice given by either party. The agency in fact was continued to December 31, 1955 and was not terminated by notice but by an agreement made early in 1954 which culminated negotiations begun some time previously when the English company decided to set up a Canadian sales subsidiary. Pursuant to the agreement terminating the agency, Doulton & Co. Ltd. paid the appellant $100,000 "in full settlement of your claim for damages for loss of rights under the agreement". In re-assessing the appellant for the 1956 taxation year the Minister added this payment to the appellant's declared income. In an appeal from the assessment the appellant, while admitting that $5,000 of the amount was income, contended that the remainder was capital. *Held:* That, except in so far as it was a consideration for services rendered to Doulton & Co. Ltd. in connection with the take-over by its subsidiary, which is admitted to be income, and except in so far as it took the place of commissions on sales of goods ordered before, but invoiced after December 31, 1955, the payment was not income from the appellant's business but was referable to the appellant's claim for loss of what it and Doulton & Co. Ltd. considered to be the appellant's interest in the goodwill and business in Doulton products in Canada. 2. That this was a capital asset of an enduring nature and the payment received in respect of its loss was accordingly a capital receipt. *Wiseburgh v. Domville* [1956] 1 All E.R. 754 at 757,760; *Commissioners of Inland Revenue v. Fleming & Co. (Machinery) Ltd.* 33 T.C. 57 at 61, referred to. PARSONS-STEINER LTD. v. MINISTER OF NATIONAL REVENUE....174

11.—*Income tax—Classification of properties—Recapture of capital cost allowance—Income Tax Act, R.S.C. 1952, c. 148, ss. 11(1)(a), 20(1)—Income Tax Regulations,*

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s. 1101(1). The respondent in partnership with another carried on a room rental business at two different places under the respective registered firm names of Alpine Rooms Reg'd. and New Frontenac Hotel and Tavern. On the sale of the Alpine property the Minister ruled that the respondent had been carrying on two separate businesses and pursuant to s. 20(1) of the *Income Tax Act* and s. 1101(1) of the *Income Tax Regulations* added to the respondent's declared income an amount to recapture the capital cost alllowance. The respondent appealed to the Tax Appeal Board on the ground that he was carrying on but one business at the two places and the recapture of capital cost allowance should be deferred until sale of the entire business. On an appeal from the Board's decision allowing the respondent's appeal to it *Held:* That Alpine Rooms Reg'd. and New Frontenac Hotel and Tavern constituted two different businesses could be inferred from the fact that each was a legal entity operating under its own firm name. A judgment creditor of the one could have no claim on the assets of the other. Their fiscal years differed, as did the characteristics in the operation of a rooming house as distinguished from that of a hotel and tavern. MINISTER OF NATIONAL REVENUE v. VICTOR TRUDEAU.....254

12.—*Income—Income tax—Land purchased in part for investment purposes later sold en bloc—Whether profit on part purchased for investment subject to tax—The Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e).* The appellant company was incorporated in September 1953 with objects which included dealing in land and holding land for investment purposes. In May 1954 it acquired title to fifty acres of land in North York Township which the syndicate of persons at whose instance the appellant was incorporated had agreed to buy in April 1953 for $250,000. The intention of the syndicate when purchasing the property was to erect apartment buildings on 35 acres of the land to be held as an investment and subdivide the remainder for single family dwelling lots. Difficulties were encountered in carrying out these plans because of the absence of water and sewer facilities and some time after the appellant company acquired title to the property it was decided to subdivide and sell as single family dwelling lots all but ten acres of the land, later reduced to five acres, which was reserved by the appellant for the apartment house project. In December the Township advised the appellant's plan of subdivision would be recommended for approval provided the appellant conveyed 11 lots to the Township and entered into a contract with it for the construction of roads and sewers, the installation of services and the payment of taxes. In February 1955 the appellant proceeded through real estate agents to sell all the

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lots in the proposed subdivision other than those required by the Township and those it had reserved for the apartment project. Most of the agreements provided that the sale would be null and void if the plan was not registered by a particular date. In July the appellant received an offer of $840,000 for the whole of the property. At this stage the agreement with the Township had not been signed nor the plan approved. There was a small flaw in title to part of the land that had to be eliminated before the plan could be registered, and the Township required a bond guaranteeing due performance by the appellant of its contract. In addition a firm estimate of the ultimate costs of the required installations could not be had. In view of these factors the appellant, after attempting without success to have the five acres reserved for the apartment building project excluded from the sale, accepted the offer. Most of the agreements for sale had become void because the plan had not been registered within the time specified. Those not so affected were repurchased by the appellant which permitted the closing of the sale in August 1955. In assessing the appellant for the year 1956 the Minister treated the whole of the profit realized from the sale of the 50 acres as income from its business. In an appeal from the assessment the appellant contended that a portion of the land so sold had been acquired and held as an investment and that the profit on that portion should be treated as a capital gain. *Held:* That at the material time the appellant was engaged in a business of dealing in land and in the course of that business sold a property which though originally in part acquired for an investmnet purpose had for trading purposes rather than for the purpose of mere realization been dealt with in its entirety as the subject matter of a trading transaction. 2. That in these circumstances the whole of the money received for the property was a trading receipt and the profit thereon a gain made in the operation of the appellant's business in carrying out its scheme for profit making. 3. That the profit was accordingly income within the meaning of the *Income Tax Act* and was properly assessed. CADILLAC CONTRACTING AND DEVELOPMENTS (TORONTO) LTD. v. MINISTER OF NATIONAL REVENUE.....258

13.—*Income—Income tax—Admissibility of evidence to vary sale price of property set out in deed—Appeal from Tax Appeal Board a trial de novo—Presumption of validity of assessment on appeal from Board's decision—Quebec Civil Code, art. 1234—The Income Tax Act, R.S.C. 1952, c. 148, s. 100(3).* On an appeal from an assessment to the Tax Appeal Board the respondent contended that the $12,000 added by the Minister to his taxable income was a non-taxable capital gain. He submitted that the sum formed part of the sale price of a property

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sold by him by notarial deed in which the consideration therein stated to be $68,000 was in fact $80,000. The $12,000 difference he claimed was paid him by the purchaser on the signing of the deed before the notary. The Minister objected to the admission of oral evidence to vary the terms of a written document. The Board allowed the respondent to call witnesses in support of his allegations. It also heard the purchaser deny the making of the $12,000 payment. On an appeal by the Minister from a finding in favour of the respondent. *Held:* That the rule under the *Civil Code* (art. 1234) which forbids the use of oral evidence to contradict or vary the terms of a valid written instrument applies only as between the parties to it and not to third parties for whom the instrument falls into the category of *res inter alios acta*. 2. That the hearing of an appeal from a decision of the Tax Appeal Board by the Exchequer Court is a trial *de novo* and it is for the court to base its decision on its own evaluation of the evidence. 3. That as the evidence adduced by the respondent failed to displace the presumption as to the validity of the assessment, or to remove the serious doubts the court entertained concerning the respondent's allegations, the appeal should be allowed and the assessment affirmed. MINISTER OF NATIONAL REVENUE v. ALBANI THIBAULT.....273

14.—*Income—Income tax—Garage mortgaged to oil company—Credits granted garage owner undertaking to deal exclusively in company's products—Capital or income—The Income Tax Act. R.S.C. 1952, c. 148, ss. 3, 4 and 139(1)(e).* The appellant, a garage and service station operator, mortgaged his property to Imperial Oil Ltd. to secure a loan of $49,600 to be used in expanding his business. The mortgage provided that the property should continue to be used as a garage and service station and that the appellant should deal exclusively in Imperial Oil products to be supplied to him at the regular price to retailers in force at the time of each purchase. In the event of appellant's failure to comply with the condition the balance of the loan was to become immediately due and payable. Subsequently the oil company advised the appellant that so long as the mortgaged premises were used for the exclusive sale of its products no interest would be charged on the loan and that at the end of each month it would allow the appellant a credit of some $275 in reduction of principal until the entire debt was liquidated. In assessing the appellant for the years 1956 and 1957 the Minister included the monthly credits as income from the taxpayer's business. An appeal from the assessment was dismissed by the Tax Appeal Board. On a further appeal to this court the appellant contended that the credits in question constituted a forgiveness of debt and were capital receipts and not profits

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from a business. *Held:* That whether the agreement between the appellant and Imperial Oil Ltd. be regarded as a conditional forgiveness of a debt secured by realty or a contract restricting the appellant's future trading rights, the monthly credits could not be considered to be profits from a business but were in the nature of capital receipts. *Commissioners of Inland Revenue v. Coia.* 38 T.C., 334, applied. *St. John Dry Dock v. M.N.R.* [1944] Ex. C.R. 186 and *Geo T. Davie and Sons Ltd. v. M.N.R.* [1954] Ex. C.R. 280, referred to. MINISTER OF NATIONAL REVENUE v. EDOUARD GALIPEAU.....284

15.—*Income—Income tax—Land purchased by private company as investment sold shortly thereafter at profit—Evidence of similar transactions—Funds distributed on winding-up deemed a dividend—Income Tax Act, R.S.C. c. 148, ss. 3, 4, 81(1) and 139(1)(e).* In 1951 D, a solicitor, acting on behalf of a private company which he later incorporated and of which he and his wife became sole owners, purchased a farm on the outskirts of Toronto for $52,000. The property was allegedly purchased as an investment and to serve as the site of the couple's future summer home but was disposed of in two separate sales in 1953 and 1954 at a substantial profit. Shortly thereafter the company was wound up, the proceeds from the sales distributed to the shareholders and the charter surrendered. The Minister treated the amount received by D as a profit from a business and added it to the taxpayer's income. D's appeal from the assessment was dismissed by the Tax Appeal Board. Following D's death his executors brought a further appeal before this Court. *Held:* That the evidence established that both prior to and after the sales now in question D had derived considerable profit from short-term purchases and sales of land in the same area. Private companies incorporated ostensibly to hold a single property for investment held it for a relatively short time and following sale the companies were promptly wound up and their assets distributed to their shareholders. This course of conduct helped to characterize the instant transaction as an undertaking in the nature of trade and served to indicate that D was engaged in a scheme of profit making. 2. That the proceeds in the company's hands following the sales in question constituted undistributed income which the Minister was justified in deeming a dividend within the meaning of s. 81 of the *Income Tax Act.* STERLING TRUSTS CORPORATION *et al* v. MINISTER OF NATIONAL REVENUE 310

16.—*Income—Income Tax Act, R.S.C. 1952, c. 148, s. 20(1) & (6)(g)—Bulk sale of assets—Proceeds of sale of depreciable property held taxable in virtue of s. 20(6)(g) of the Income Tax Act—Appeal dismissed.* Appellant disposed of its business assets and

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good-will to the Toronto Transit Commission for the sum of $450,000 without allocating any portion of the total purchase price to the fixed assets, buses, equipment and goodwill respectively. It contended that only $65,187.53 could be considered as paid for the buses, the depreciable assets of the business. The respondent assessed the appellant for $172,300 of the purchase price relying on the evidence of two expert valuers who had advised the Toronto Transit Commission that in their opinion the buses were worth $172,300. An appeal to the Tax Appeal Board was dismissed and appellant now appeals to this Court. *Held:* That $172,300 is that part of the total consideration of $450,000 that can reasonably be regarded as being the consideration for the disposition of the buses and this amount is deemed to be the proceeds of the disposition of the appellant's depreciable property within the meaning of s. 20(1) of the Act "irrespective of the form or legal effect of the contract or agreement" between appellant and the Toronto Transit Commission. 2. That the respondent was right in assessing appellant as he did and the appeal must be dismissed. WEST YORK COACH LINES LTD. v. MINISTER OF NATIONAL REVENUE.....323

17.—*Income Tax Act, R.S.C. 1952, c. 148, ss. 29, 139(4)—Appellant not "ordinarily resident" in Canada from date of his removal to United States of America though his family remained in Canada to end of that year—Appeal allowed.* Appellant, a United States citizen employed by a corporation of that country was moved to Toronto, Ontario by his employer in 1954. He purchased a house in Toronto and lived there with his wife and family until he was promoted to a higher position in the company in July 1957. He left Toronto for Minneapolis on August 2, 1957 taking only his personal effects with him. As he was unable to sell his house at that time he left his wife and children in Toronto in order that the house would not be vacant and so easier to sell. He resigned his club membership in Toronto. The house was sold in February, 1958, at which time his family rejoined him in the United States. Between August 2, 1957 and the end of the year 1957, the appellant was in Canada only three times, for a week-end on his way overseas, for a few days on his return and for a week at Christmas. The respondent assessed appellant for tax on his full 1957 income, from which assessment he appealed to this Court. *Held:* That the appellant ceased to be resident or "ordinarily resident" in Canada in August 1957 despite the fact that his wife and son remained in Canada until the sale of his house, and therefore is entitled to the deductions allowed by s. 29 of the *Income Tax Act,* R.S.C. 1952, c. 148 from August 2, 1957 to the end of the year. EDWIN L. SCHUJAHN v. MINISTER OF NATIONAL REVENUE.....328

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18.—*Income Tax Act, R.S.C. 1952, c. 148, s. 6(1)(c)—Partnership—Capital or income —Amount paid for relinquishing right to receive profits of partnership held a capital receipt—Appeal allowed.* In 1949 appellant and four other persons entered into an agreement with one Purcell to lend to Purcell a sum of money with which to purchase a seat on the Toronto Stock Exchange and to provide working capital for a stock brokerage business. The agreement provided for payment to each of the five lenders of a percentage of the annual net profits of the business after an allowance to Purcell and also that they were not to be considered as partners in the business but only as lenders. On the first day of February, 1956 the arrangement was rescinded by an agreement between the lenders and Purcell by which Purcell agreed to pay to the lenders the amount of the loan outstanding, the increase in value of the seat on the Exchange, the share of the lenders in the profits of the business for the fiscal year ending March 31, 1956 and the share of the lenders in the goodwill of the business. The Minister assessed the appellant for tax on his share of the profits of the brokerage business for the 1956 fiscal period. An appeal to the Tax Appeal Board was dismissed and the appellant appealed to this Court. The Court held that the arrangement between the parties was that of a partnership and not merely one involving the lending of money, and that the partnership must be considered as dissolved on February 1, 1956 the date of the agreement rescinding the 1949 agreement. *Held:* That the amount paid to appellant for relinquishing his right to receive profits of the partnership was a capital receipt and not income. JOSEPH SEDGWICK v. MINISTER OF NATIONAL REVENUE.....337

19.—*Income—Income tax—Income or capital gain—Land bought for market garden resold—Other land sales—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e).* The appellant with two others in July 1955 purchased from B for $18,500 forty acres of farm land on the outskirts of Edmonton for the purpose of a market garden. In December one of the purchasers was asked by a real estate agent if he would be willing to sell the land at $2,000 per acre. As a result of this conversation the purchasers decided not to proceed with the garden scheme but simply to hold the land. In October 1956 one of the purchasers died and the following December the survivors accepted an offer of $80,000 for it. In the period between the purchase and sale both appellants with other associates had engaged in several speculative ventures in the purchase and sale of real estate in and about Edmonton. The Minister treated the profit realized on the sale of the B property as income from a business, and, on the appellants' appeal from the assessment, contended that the purpose

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for which the land was acquired changed after the purchase and that, as the sale was made when the appellants were actively trading in land, the profit from the sale should be regarded as made in the course of trading. *Held:* That at the time of purchase the appellants had no other purpose in mind than to establish a market garden. When they realized that the land's value made it impractical to operate it as such they made no attempt to sell and it was only after the death of their associate that they accepted the $80,000. In these circumstances there was nothing to characterize their action as trading in land and the profit realized simply represented an enhancement in value on the realization of a capital asset. 2. That it did not follow from the mere fact that the appellants had engaged in transactions of a trading nature in real estate while holding the property in question that the sale thereof must be regarded as a trading transaction rather than a mere realization of value on sale of an investment. Appeals allowed and assessments varied accordingly. DONALD QUON v. MINISTER OF NATIONAL REVENUE....353
LEE K. YUEN v. MINISTER OF NATIONAL REVENUE.....353

20.—*Income—Income Tax Act, R.S.C. 1952, c. 148, ss. 12(1)(a), 14(2)(3), 85(e), 139(1)(w), 2(a) and 125(1)—Bulk sale of a business including stock on hand or so called inventory —Taxability of proceeds from such sale—Deductibility of cost of such inventory—"An outlay or expense . . . made or incurred . . . for the purpose of gaining or producing income . . . from a business"—Deductibility of outlay or expense under s. 12(1)(a)—Duty on taxpayer to open and close out its inventory at the beginning and end of its taxation year—Appeal dismissed.* The respondent, under the name of Consolidated Oka Sand & Gravel Co. Limited, was engaged for many years mainly in the business of dredging sand from two water lots in the Lake of Two-Mountains, which it transported in its own fleet to other leased properties located at Ville LaSalle, in the Parish of Lachine, Quebec, for storage and distribution purpose. It also owned and managed certain revenue-producing properties which it developed on McCord St., in the City of Montreal. On March 14, 1955, some time prior to the end of its taxation year, by a bulk or slump sale transaction it disposed of its entire sand business, including its name and good will, for $375,000. On the above date the respondent had on hand 40,000 tons of sand which was included in the bulk sale price and for which the purchaser had agreed to pay one dollar a ton. The cost of production was $52,808.90. The Minister of National Revenue, by reassessment, added the $40,000 so received to the Company's taxable income. The Company's appeal against the assessment was maintained by the Tax Appeal Board. The Minister of National Revenue appealed

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from the said decision. Counsel for the appellant, at the hearing, conceded that the sum of $40,000 in issue constituted a capital receipt, and not profit on the sale of sand, as claimed in the Minister's assessment, but took the position that it was nevertheless taxable on the ground that the production cost of the 40,000 tons amounting to $52,808.90, reduced to the equivalent of its fair market value as provided by s. 14(2), should be charged against the bulk sale proceeds which amounted to $40,000. In order to arrive at the above conclusion, the appellant looked upon the 40,000 tons as inventory the status of which should be determined as of the date immediately preceding the bulk sale to the appellant. *Held:* That no part of the receipt from the bulk sale was a receipt from the appellant's business and was not liable to tax. *Frankel Corporation Ltd. v. The Minister of National Revenue* [1959] S.C.R. 713, followed. 2. That the cost of producing the sand which was sold in bulk was an outlay or expense made or incurred by the taxpayer for the purpose of gaining or producing income and was accordingly deductible under s. 12(1)(*a*) of the Act. 3. That the cost of the 40,000 tons in question having been incurred in the ordinary course of the Company's business it should be deducted only from sales realized in a like manner. 4. That insofar as inventory is concerned the only obligation on the taxpayer is to open and close out its inventory at the beginning and end of its taxation year, and as there was no inventory on hand at the end of the 1955 taxation year, s. 14(2) of the Act would not be applicable. MINISTER OF NATIONAL REVENUE v. MCCORD STREET SITES LTD.....361

21.—*Income tax—Income Tax Act, R.S.C. 1952, c. 148, ss. 12(1)(a) and 12(1)(b)—Deductibility of cost of acquiring a construction contract by a contractor—Outlay or expense on account of capital or outlay or expense for purpose of gaining income—Appeal allowed.* Appellant was incorporated for the purpose of constructing pipe lines as a contractor. It acquired the interest of Canadian Pipe Line Construction Co. Ltd. in a joint venture together with some equipment at a total cost of $325,000. The equipment was valued at $95,000 and the Court found that the sum of $230,000 had been paid for the acquisition of the contract to do the construction work. The appellant completed the work called for and in its income tax return for the taxation year deducted the payment of $230,000 to Canadian Pipe Line Construction Co. Ltd. The respondent disallowed the deduction and re-assessed the appellant accordingly. On appeal to this Court the respondent contends that the payment constituted an outlay or expense on account of capital and was therefore barred by ss. 12(1)(*a*) and 12(1)(*b*) of the *Income Tax Act*, and, alternatively, that the appellant had not

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merely bought a construction contract but had actually purchased an interest in a joint venture or partnership which should be considered as a capital asset. *Held:* That the $230,000 was laid out for the purpose of earning the income within the meaning of s. 12(1)(*a*) of the *Income Tax Act* since appellant, a pipe line contractor, in order to earn a profit must first acquire construction contracts before it would be able to complete contracts profitably by performing the work. 2. That no asset or advantage of an "enduring" nature was acquired by appellant and so the deduction was not barred by s. 12(1)(*b*) of the Act. 3. That the acquisition of an interest in a joint venture by a construction company was not the acquisition of a capital asset because the construction company was in the business of acquiring such interests. WILLIAMS BROTHERS CANADA LTD. v. MINISTER OF NATIONAL REVENUE.....375

22.—*Income tax—Income War Tax Act, R.S.C. 1927, c. 97, s. 3—Income Tax Act 1948, S. of C. 1948, c. 52, ss. 3, 4, 127(1)(e)—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 139(1)(e)—Profits from mortgages purchased at a discount—Capital gain or income.* The respondent taxpayer who for some years had been engaged in a soap manufacturing operation and in earlier years had had a wide experience in different fields of business activity and in managing estates as official administrator, in 1943 or 1944 was offered at a discount some mortgages and agreements of sale of private homes in Vancouver. He bought a few of these and having found after a time that they were a satisfactory way to invest his money he converted his other investments into cash and invested the proceeds as well as current savings in mortgages and agreements of this kind. Between 1944 and 1954 he purchased a total of 309 mortgages and agreements from those offered to him by various real estate agents without solicitation on his part all at a discount. One hundred and thirteen of these mortgages and agreements of sale were paid off during the years in question and the sums realized from them were treated by the Minister of National Revenue as income in the hands of the respondent and assessed accordingly. The respondent contended that such discounts should be treated as capital increments. An appeal to the Tax Appeal Board was allowed on the ground that the reassessment made for the years 1946 to 1951 were invalid because they were made beyond the time limit prescribed by the statutes and that the discounts received in all the years 1946 to 1954 were accretions of capital. The Minister appealed to this Court and on the hearing of the appeal counsel for the respondent admitted the right of the Minister to make the reassessments when they were made. The securities purchased were not of the kind in which mortgage companies were interested since,

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though constituting a first charge the principal amount in each case represented up to two-thirds of the value of the property and the companies were unwilling to invest beyond 45 to 50 per cent of the value and also because the mortgage companies were more interested in larger mortgages which met their requirements. The taxpayer was not the lender in any of these transactions and never sold or disposed of any of the mortgages except on very rare occasions for special reasons. *Held:* That the discounts realized by the respondent in the years in question were simply enhancements of value on the realization of investments and not gains made in an operation of business in carrying out a scheme for profit making. 2. That the gains realized on the discounts in the years 1946, 1947 and 1948 were not profits from a trade or business within the meaning of the definition of income in s. 3 of the *Income War Tax Act* R.S.C. 1927, c. 97 nor were the gains realized on discounts in the years 1949-1954 inclusive income within the meaning of the *Income Tax Acts* 1948, S. of C. 1948, c. 52 and R.S.C. 1952, c. 148. MINISTER OF NATIONAL REVENUE v. WILLIAM HEDLEY MACINNES...385

23.—*Income tax—Income Tax Act, 1948, S. of C. 1948, c. 52, ss. 3, 5, and 16—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 15 and 16(1)—Income or capital receipts—Commissions payable under agreement—Payment on termination of contract—Payments for assignment of rights to commissions—Payments commuting rights to commissions—Commissions in lump sum—Taxation of commissions not received—Whether payments taxable—Appeal allowed—Cross-appeal dismissed.* Appellant introduced M to a United States manufacturer of parking meters and as a result M obtained an exclusive license under a patent to manufacture and sell these parking meters in Canada. In August 1950, pursuant to the provisions of an earlier agreement between them, the appellant became exclusive sales agent for M in the Province of Quebec and part of Ontario on a commission basis and became entitled on the termination of the agency to a commission of 2½ per cent on sales made in the same territory payable during the life of the appellant so long as the patent existed. In July 1951 M purported to terminate the agency by a notice given pursuant to the agreement and a dispute having arisen as to the validity of such termination, the appellant and M in October 1951 entered into another agreement by which the termination of the agency was confirmed but it was further provided that the appellant should receive $3,750 in instalments and a commission in respect of certain pending sales and his right to the commission of 2½ per cent during his life for the term of the patent was confirmed. Of the $3,750, $1,750 was paid to the appellant in 1952, one of the taxation years with which the appeal is concerned.

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In the same year the appellant assigned his rights to payment of the commission on the pending sales to A.M.I. in consideration of an immediate payment of $12,000 and 42 per cent of the commissions in excess of that sum. Under this assignment appellant received in 1952 payments of $12,000 and $1,470 and in 1953 received $896.27. In 1953 appellant by a further agreement released his rights to future payments of the 2½ per cent commission in return for an immediate payment of $5,000. The Minister assessed all amounts paid to the appellant under these agreements as subject to tax and on the assumption that s. 16(1) of the *Income Tax Act* applied to the appellant's transaction with A.M.I. also assessed as income of the appellant amounts representing the 58 per cent of the commissions in excess of $12,000 retained by A.M.I. Appellant's appeal to the Tax Appeal Board succeeded with respect to the inclusion in his income of the amounts retained by A.M.I. but in other respects failed. He thereupon appealed to this Court and the Minister cross-appealed seeking to have the assessments restored. *Held:* That the $1,750 received in 1952 under the 1951 agreement was not a profit from appellant's business but a capital receipt, and was not subject to tax as income. 2. That the sums of $12,000 and $1,470 received from A.M.I. in 1952 and $896.27 in 1953 were income receipts and subject to tax. 3. That the right of the appellant to the 2½ per cent commission was a right of a capital nature and the $5,000 received by appellant for the release of such right was also capital. 4. That s. 16(1) of the *Income Tax Act* did not apply to the appellant's transaction with A.M.I. and that the cross-appeal failed. ALEX MILLER v. MINISTER OF NATIONAL REVENUE.....400

24.—*Income Tax—Income Tax Act, R.S.C. 1952, c. 148 ss. 11(1)(a), 12(1)(a)(b)—Income Tax Regulations, Schedule B, Class 8—Purchase of accountant's business, goodwill and list of clients—Payment deductible under s. 12(1)(a) of the Income Tax Act—List of accounts not depreciable as a tangible asset.* Appellant, a chartered accountant practising in Winnipeg, by an agreement made in 1954 purchased from a retiring accountant "all the right, title and interest of the vendor in and to the goodwill of the accounting business" carried on by the vendor including the right to use the firm name. The agreement provided *inter alia* for the delivery by the vendor of a list of his clients showing the regular annual fees charged by the vendor for the usual annual audit and that the appellant should pay to the vendor as the price of such goodwill seventy per cent of the aggregate of the regular annual fees so charged. The seventy per cent amounted to $17,153.50 and this sum was paid by appellant who in computing his income for the year deducted it as an expense. The deduction having been dis-

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allowed by the respondent the appellant appealed claiming that the amount was an expense incurred for the purpose of gaining or producing income from his business and not an outlay of capital. Alternatively he claimed that he was entitled to a deduction of capital cost allowance in respect of the list of clients. *Held:* That the expenditure was not of a recurring nature but was made once and for all with a view to bringing into existence an advantage for the long term benefit of the appellant's practice and was an outlay of capital deduction of which in computing income is prohibited by s. 12(1)(*b*) of the *Income Tax Act*. 2. That the goodwill for which the $17,153.50 had been paid was not a tangible capital asset within the meaning of the capital cost regulations made under s. 11(1)(*a*) of the *Income Tax Act* and that the appellant was not entitled to a deduction of capital cost allowance in respect of it. Nor was the appellant entitled to deduct capital cost allowance in respect of the list of accounts, as nothing had been paid for it and there was no capital cost of it to the appellant to which s. 11(1)(*a*) could apply. IRVIN CHARLES SCHACTER v. MINISTER OF NATIONAL REVENUE.....417

25.—*Income tax—The Income Tax Act, 1948, S. of C. 1948, c. 52 ss. 3, 4, and 127(1)(e)—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, and 139(1)(e)—Bonus on mortgages—Mortgage discounts—Capital gains or income—Taxpayer engaged in speculative or adventurous undertakings in nature of trade—Appeal allowed.* Respondent, engaged in the wholesale produce business, from time to time purchased mortgages recommended to him by his solicitor at a discount and also made direct loans to mortgagors receiving a bonus on such. All these mortgages were for short terms and most were second mortgages on real property, some were second chattel mortgages. The Minister of National Revenue assessed the respondent for income tax on the discounts and bonuses realized on 31 on these transaction for the years 1948 to 1953 inclusive. An appeal to the Tax Appeal Board was allowed and from that decision the Minister appeals to this Court. *Held:* That the discounts and bonuses realized by the respondent are income and subject to tax. 2. That while the respondent could not be said to be operating a business in the ordinary sense of the term he was engaged in speculative or adventurous undertakings of a trading nature within the provisions of s. 139(1)(*e*) of the *Income Tax Act*. 3. That respondent's mortgage dealings were short-term profit-making transactions frequently repeated, highly speculative and could not be regarded as ordinary or normal investments. MINISTER OF NATIONAL REVENUE v. MAX WOLFE.....428

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26.—*Excise—Sales tax—Exemption—Meaning of term "portrait photographers" under the Excise Tax Act and Old Age Security Act—Excise Tax Act, R.S.C. 1952, c. 100, ss. 30, 34(2), Schedule III, as amended by S. of C. 1960, c. 30—Old Age Security Act, R.S.C. 1952, c. 200 as amended by S. of C. 1959, c. 14.* The Crown brought action to recover sales tax and penalties from the defendant under the provisions of the *Excise Tax Act*, R.S.C. 1952, c. 100, as amended, and the *Old Age Security Act*, R.S.C. 1952, c. 200 as amended, on sales affected between December 1959 and April 1960. The defendant, a company carrying on business of photographing farms from the air and selling such photographs to the farm and home owners, claimed exemption under the provisions of s. 34(2) of the *Excise Tax Act* and Regulation 11 thereof, which regulation provides exemption from sales tax to portrait photographers who sell exclusively to the consumer or user. By petition of right the above-named defendant brought action to recover from the Crown sales tax paid by it on such photographs made by it between May and December 1959. The two actions were tried together. The sole point at issue in both cases was as to whether the defendant was a "portrait photographer" within the meaning of the *Excise Tax Act*, regulation 11. *Held:* That although one meaning of "portrait" (in English) is the representation of an object, the predominant meaning, and that attributed to it by usage of the trade, is that of a representation of a person, either of his face or his whole person. 2. That as there is no definition of the word "portrait" in the *Excise Tax Act* or the *Regulations*, and as it is not defined in any other acts in *pari materia*, it must be given the meaning ascribed to the word by persons familiar with the subject matter of the legislation. 3. That in construing the words "portrait photography" the court must apply the rule that an exemption provision in a statute must be given its strictest meaning in order to give the benefit to the narrowest group possible and on applying the rule the court concludes that the defendant company's operations do not fall within the exemption provided under the term "portrait photography". HER MAJESTY THE QUEEN v. CONTINENTAL AIR PHOTO LTD. 461

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27.—*Income—Income tax—Payment to real estate trader to relinquish option—Capital or revenue—The Income Tax Act, R.S.C. 1952, c. 148, ss. 2(3), 3, 4, 139(1)(e)—Civil Code, arts. 1476, 1477.* Appellant obtained from G an option to purchase certain farm land. The option stipulated *inter alia* that it must be accepted not later than May 28, 1956, and be accompanied by a deposit of $25,000. G died a few days later and the appellant on May

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25, 1956, forwarded his acceptance in writing together with a certified cheque of $25,000 payable to G's estate. G's personal representatives refused to honour the option and after negotiation appellant surrendered his rights thereunder on payment of $50,000 and the return of his deposit. In re-assessing the appellant for the year 1956 the Minister added $50,000 to the appellant's declared income. An appeal from the assessment was dismissed by the Tax Appeal Board. On a further appeal to this court the taxpayer submitted that the sum in question was paid for the surrender of a right separate and distinct from the land and was neither profit or income but a capital sum. The Minister contended that payment for breaches of contract are capital receipts when received as compensation for loss of capital assets but are income from a business when received in lieu of profits from a business. That the appellant was a trader in real estate and had he acquired the optioned land it would have constituted stock in trade and therefore what he received was compensation for loss of inventory. *Held:* That the appellant was engaged in the real estate business in the widest sense of the term. 2. That transactions commonly called "options" in the Province of Quebec are governed by the provisions of the *Civil Code* and that, as provided by article 1471, G's estate was legally entitled to revoke the option by returning appellant his deposit and paying him double that amount. 3. That the resulting gain was one which any regular dealer in real estate would experience in the ordinary course of his business and, as the appellant failed to prove the instant transaction occurred outside the ordinary course of such business, the $50,000 payment constituted taxable income in his hands. DAVID MILLER v. MINISTER OF NATIONAL REVENUE.....453

RULE 29, GENERAL RULES AND ORDERS IN ADMIRALTY.

See SHIPPING, No. 2.

RULES 14, 15, 16, 20(d), 21, 24, GENERAL RULES OF THE EXCHEQUER COURT IN ADMIRALTY.

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See REVENUE, No. 26.

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SHIPPING—

1. Action for damage to ship occasioned by negligence in dry-docking. No. 4.
2. Admiralty Act, R.S.C. 1952, c. 1, ss. 3, 12, 18(3)(4). No. 3.
3. Appeal dismissed. No. 5.

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4. Appeal from order of District Judge in Admiralty dismissed. No. 3.
5. Bills of Lading Act, R.S.C. 1952, c. 16. No. 3.
6. Collision in Quebec City Harbour. No. 5.
7. Contravention of Rules 29, 25 and 22 of the International Rules of the Road. No. 5.
8. Court considers all material before in on motion to set aside order for service ex juris. No. 3.
9. Damage to cargo. No. 3.
10. Damage to pipeline caused by negligence of defendant ship. No. 6.
11. Impleading foreign sovereign state. No. 1.
12. Interest allowed as part of damages. No. 6.
13. International law. No. 1.
14. Jurisdiction. No. 3.
15. Motion dismissed. No. 2.
16. Motion to strike out defendants. No. 2.
17. Negligence of defendant ship sole cause of collision. No. 5.
18. Notice. No. 3.
19. Practice. No. 2.
20. Rule 29, General Rules and Orders in Admiralty. No. 2.
21. Rules 14, 15, 16, 20(d), 21, 24, General Rules of the Exchequer Court in Admiralty. No. 3.
22. Service of writ out of country. No. 3.
23. Sovereign immunity. No. 1.
24. Sufficiency or insufficiency of affidavit of service. No. 3.
25. Undertaking by plaintiff to be responsible for damage to ship and cargo resulting from dry-docking with cargo on board or distribution of cargo does not exempt defendant from liability for loss suffered by negligent dry-docking. No. 4.
26. Vessels arrested on behalf of private suitor. No. 1.
27. Vessels in Canadian port sold to Republic of Cuba. No. 1.
28. Water Carriage of Goods Act, 1936, R.S.C. 1952, c. 291. No. 3.
29. Writ of summons. No. 3.

SHIPPING—*International law—Sovereign immunity—Vessels in Canadian port sold to Republic of Cuba—Vessels arrested on behalf of private suitor—Impleading foreign sovereign state.* Banco Cubano del Commercio, a Cuban corporation, in August, 1958 purchased at Montreal eight steamships then lying in the Port of Halifax. On the same date it signed a lease-purchase agreement with the respondent, another Cuban corporation, which provided for the operation of the ships by the latter with

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an option to purchase. On October 31, 1958 the respondent, claiming the bank had repudiated delivery and usurped its rights under the contract, declared it a nullity and surrendered possession of the ships to an agent of the bank but reserved the right to claim damages for breach of contract. On June 9, 1959, the bank sold the ships to the Republic of Cuba. On August 4, 1960 the respondent instituted proceedings *in rem* in the Nova Scotia Admiralty District by a writ directed to the owners and all others interested in the defendant vessels and applied for and was granted a warrant for the arrest of the vessels still in Halifax. Counsel for the appellant entered an appearance under protest on the ground that the court had no jurisdiction and moved to set aside the writ and the warrant for arrest and service thereof on the grounds the vessels were public national property of and in the possession of the Republic which could not be impleaded; and further that by the agreement relating to the use and hire of the ships the respondent expressly submitted itself and all questions relating to the agreement to the jurisdiction of the Cuban courts. Pottier D.J.A. dismissed the application. On an appeal to this Court *Held:* That having regard to the nature of the appellant's claim to the ownership of and rights of possession and control in the defendant vessels the Republic of Cuba was in fact impleaded and was intended by the respondent to be impleaded. *The Cristina* [1938] A.C. 485 at 492. 2. That a foreign government, claiming that its interest in property will be affected by a judgment in an action to which it is not a party and in which it alleged it is indirectly impleaded, is not bound as a condition of obtaining immunity to prove its title to the interest claimed, but it must produce evidence to satisfy the court that its claim is not merely illusory, nor founded on a title manifestly defective. *Juan Ysmael & Co. Inc.* v. *Indonesian Government* [1955] A.C. 72, applied. 3. That on the evidence the appellant's claim to ownership and right of possession of the defendant vessels is not illusory nor founded on a title manifestly defective. 4. That the defendant vessels on August 4, 1960, were the property of the Republic of Cuba. 5. That the rule of sovereign immunity extends to property of a foreign sovereign or state even if that property be used for commercial purposes. The rule as stated by Lord Atkin in *Compagnia Naviera Vascongado* v. *S.S. Cristina* [1938] A.C. 485 at 490, applied. 6. That the Court having come to the conclusion that conflicting rights have to be decided in relation to the claim of the Republic of Cuba, the writs and warrants of arrest and service thereof must be set aside as the Court is without jurisdiction to entertain the action. *Juan Ysmael & Co. Inc.* v. *Indonesian Government* (*supra*) followed. THE REPUBLIC OF CUBA v. FLOTA MARITIMA BROWNING DE CUBA, S.A. *et al* 1

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2.—*Practice—Rule 29, General Rules and Orders in Admiralty—Motion to strike out defendants—Motion dismissed. Held:* That where the plaintiff is not certain which defendant or combination of defendants caused the damage complained of which arose out of the same matter all defendants may be joined in the same action as provided in Rule 29 of the General Rules and Orders of the Exchequer Court in Admiralty. CANADIAN BRINE LTD. v. NATIONAL SAND & MATERIAL CO. LTD.....131

3.—*Damage to cargo—Writ of summons—Jurisdiction—Service of writ out of country—Notice—Admiralty Act, R.S.C. 1952, c. 1. ss. 3, 12, 18(3)(4)—Rules 14, 15, 16, 20(d), 21, 24, General Rules of the Exchequer Court in Admiralty—Sufficiency or insufficiency of affidavit of service—Court considers all material before it on motion to set aside order for service ex juris—Bills of Lading Act, R.S.C. 1952, c. 16—Water Carriage of Goods Act, 1936, R.S.C. 1952, c. 291—Appeal from order of District Judge in Admiralty dismissed.* On March 2, 1955, two Japanese corporations commenced an action in the British Columbia Admiralty District as plaintiffs against the Panamanian Steamship *Panaghia*, against Anglo Canadian Shipping Company Limited the charterer of the ship and against Compania Navegacion Sappho S.A., a Panamanian corporation, the owner of the ship, claiming damages to a quantity of pulp carried on the ship from British Columbia ports to Japan. Service of the writ of summons was made in British Columbia on the charterers who entered an appearance and filed a defence. The ship was not arrested but on April 5, 1955, on the plaintiffs' application, leave was granted by Mr. Justice Sidney Smith, D.J.A. to plaintiffs to issue a concurrent writ of summons against the defendant Compania de Navegacion Sappho S.A. and to serve notice of such writ in the Republic of Panama. Such concurrent writ was issued and on May 16, 1955 notice of the writ of summons was delivered to the resident agent of the defendant company in Panama. On the same day the agent sent the notice to New York where, largely by chance (because it was sent to the wrong agents) it reached agents of the defendant company who thought it had been served by mail and upon being advised by British Columbia solicitors that service by post was invalid did nothing about the matter. On March 22, 1957, plaintiffs obtained an interlocutory judgment by default and on July 15, 1957, a copy of the judgment was forwarded to the defendant company's agents in New York. Nearly a year later the plaintiffs proceeded with a reference to assess damages and counsel, instructed by the company's New York agents, appeared on behalf of the company and stated he reserved all defences available to

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the company. On October 14, 1958, motions were launched on behalf of the company first, for an order setting aside the service and all subsequent proceedings and alternatively setting aside the judgment and giving leave to appear and defend and second, for an order setting aside the writ of summons on the ground that the Court had no jurisdiction to issue it. Smith, D.J.A. ordered that the default judgment be set aside and that the defendants have leave to defend but upheld the service made on the defendant company and he refused the application to set aside the writ of summons. The defendant company now appeals to this Court from the refusal to set aside the service of the writ and subsequent proceedings. *Held:* That the appeal should be dismissed. 2. That Rule 24 of the General Rules and Orders of the Exchequer Court of Canada in Admiralty provides that notice in lieu of service shall be given in the manner in which writs of summons are served and the manner of service of a writ of summons upon a corporation is provided for by Rules 14, 15 and 16 and though the affidavit of service made by the solicitor who delivered the notice falls short of showing that there was valid service under Rule 14, service of Panamanian process upon the resident agent would have been valid service upon the appellant and the Panamanian law came within the words of Rule 15; and further it was not open to the appellant to ignore the service entirely and much later to ask the Court to set it aside. 3. That the responsibility of not knowing the true facts as to the delivery of the notice rested on the appellant, and the Court was justified in refusing to set the service aside merely because of the alleged insufficiency or irregularity in the manner in which it was carried out. 4. That the plaintiffs were justified in bringing action against both defendants as there appeared to be uncertainty as to who were the actual contracting parties. 5. That the action was properly brought against the charterers and the fact that the cargo was loaded in British Columbia and that the provisions of the *Water Carriage of Goods Act, 1936* applied, were sufficient grounds for the Court to entertain the action against the appellant. IWAI & CO. LTD. *et al* v. THE SHIP *Panaghia et al*.....4

4.—*Action for damage to ship occasioned by negligence in dry-docking—Undertaking by plaintiff to be responsible for damage to ship and cargo resulting from dry-docking with cargo on board or distribution of cargo does not exempt defendant from liability for loss suffered by negligent dry-docking.* The action is for damages done to the hull of plaintiff's ship the *Extavia* in a dry-dock operated by the defendant at the northerly end of the Welland Canal. Prior to the dry-docking the ship (loaded with a cargo of well over 2,000 tons) on a voyage from Milwaukee to Montreal grounded and

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it was to have ascertained any damage occasioned by this accident that the ship was taken to the defendant's dry-dock. Defendant did not wish to deal with a loaded ship and after some negotiations plaintiff company sent defendant a telegram reading as follows: "We confirm telephone agreement Friday to assume responsibility for damage to vessel and cargo which may result from dry-docking with cargo on board or distribution of cargo". In docking the ship was not docked squarely with the keel mid-way on the keel blocks which had been placed there to support it and in the result there was certain buckling along the underbody of the hull from about midship forward to the stem which eventually had to be repaired and it is for the cost of these repairs that the action is brought. The defendant contends that it was released from all liability for any damage by virtue of the telegram sent it by plaintiff's officer. *Held:* That the damage to the ship was not caused by the presence of the cargo on board but was caused by the faulty docking and neglect to take precaution to sight adequately and carefully what the position of the ship was before it was lowered to the blocks. 2. That the defendant is not exempted from liability for the negligence found by the Court by virtue of the telegram since to have the exemption go that far it must be shown that the negligence complained of was a direct result from the presence of the cargo on board or from its peculiar distribution. AMERICAN EXPORT LINES INC. v. PORT WELLER DRY-DOCK LTD.....188

5.—*Collision in Quebec City Harbour—Negligence of defendant ship sole cause of collision—Contravention of Rules 29, 25 and 22 of the International Rules of the Road—Appeal dismissed.* Respondent recovered judgment against the appellants for damages resulting from a collision between its vessel and that of the appellants. From that judgment the defendants now appeal to this Court. *Held:* That on the facts as found by the learned trial Judge the appeal must be dismissed. 2. That the collision and resulting damage were caused solely by the negligence and fault of those in charge of appellant ship in contravening rules 29, 25 and 22 of the *International Rules of the Road* in that they failed to keep to the side of the fairway or mid-channel which lay on their starboard side, in failing to post a look-out on the bow of the vessel and in altering the course of their vessel to port which brought her on a course which crossed that of plaintiff vessel. 3. That this court sitting in appeal in admiralty matters will not interfere with the judgment of the lower court as regards pure questions of fact or the quantum of damages unless it appears clearly erroneous. The S.S. *Ethel Q v. Adelard Beaudette*, 17 Ex. C.R. 505 applied. THE SHIP *Argyll* AND HER OWNERS v. THE OWNER OF THE SHIP *Sunima*, AKSJE SELSKAP I.M.A.....293

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6.—*Damage to pipeline caused by negligence of defendant ship—Interest allowed as part of damages.* The action is brought to recover damages suffered by the plaintiff which serviced, repaired and maintained a portion of a pipeline running from Windsor, Ontario to Detroit, Michigan under the Detroit River. The pipeline was damaged by one of the flukes of an anchor of the defendant ship. The defendants admitted that the anchor fouled a portion of the pipeline in the vicinity of the place of anchorage but contend that such fouling was without negligence and that the ship was forced to anchor where it did due to weather conditions and the visibility at the time and also that it was necessary to use both bow and stern anchors due to a heavy down current and ice conditions. The plaintiff pleads negligence, trespass and nuisance. The Court found that the captain of the defendant ship anchored it without any care or regard to any signs which might be available to him which would indicate that he was anchoring in an area where he might do serious damage, and without regard to the rights of others in that area. It was also negligence on the part of the officers of the defendant ship to direct that the anchor be raised and lowered until the obstruction which it had picked up fell off. *Held:* That the plaintiff is entitled to recover the cost of replacing the pipeline but not that incurred by steps taken to anchor it securely to the bottom of the river by means of concrete weights. 2. That there is a discretion in a Court of Admiralty to award interest whether the rights dealt with arose *ex contractu* or *ex delicto* and such interest is not granted as something apart from the damages but as an integral part of them and the negligence exhibited by the master and officers of the defendant ship is so gross in its character to warrant the inclusion of interest as part of the damages to which the plaintiff is entitled. CANADIAN BRINE LTD. v. THE SHIP *Scott Misener* AND HER OWNERS.....441

"SIMILAR".

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SOVEREIGN IMMUNITY.

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SUBSTANCE CLAIM MUST BE LIMITED TO THAT SUBSTANCE WHEN PRODUCED BY PROCESS FOR ITS PREPARATION CLAIMED AND PARTICULARLY DESCRIBED OR AN OBVIOUS CHEMICAL EQUIVALENT.

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"SUCCESSION."

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SUFFICIENCY OR INSUFFICIENCY OF AFFIDAVIT OF SERVICE.

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TAXABILITY OF PROCEEDS FROM SUCH SALE.

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TAXPAYER ENGAGED IN SPECULATIVE OR ADVENTUROUS UNDERTAKINGS IN NATURE OF TRADE.

See REVENUE, No. 25.

TO VALIDATE PRODUCT CLAIM PROCESS CLAIM MUST BE VALID.

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TRADE MARKS—

1. "Distinctive". No. 1.
2. Infringement. No. 1.
3. Passing off. No. 1.
4. "Similar". No. 1.
5. Trade Marks Act, S. of C. 1952-53, c. 49, ss. 2(b), (f), 6(1)(2)(5), 7, 18(1)(a)(b), 18(2), 19, 20. No. 1.
6. Unfair Competition Act, R.S.C. 1952, c. 274, s. 2(f)(k)(o). No. 1.
7. Whether "Royal" a "common laudatory epithet" or "clearly descriptive or misdescriptive" work mark. No. 1.
8. Whether trade marks "Royal Gold" and "Royal" confusing. No. 1.

TRADE MARKS—*Infringement—Passing off—Whether trade marks "Royal Gold" and "Royal" confusing—Whether "Royal" a "common laudatory epithet" or "clearly descriptive or misdescriptive" work mark—"Similar"—"Distinctive"—Trade Marks Act S. of C. 1952-53, c. 49, ss. 2(b), (f), 6(1)(2)(5), 7, 18(1)(a)(b), 18(2), 19, 20—The Unfair Competition Act, R.S.C. 1952, c. 274, s. 2(f)(k)(o).* In 1953 the plaintiff, who had been using the word "Royal" as a trade mark extensively and continuously in association with its products since 1922, obtained registration of the word as a trade mark for use in association with ice cream, ice cream sundries, milk, cream, buttermilk, cottage cheese, chocolate diary milk, evaporated milk and condensed milk. The defendant in 1957 registered the trade mark "Royal Gold" for use in association with butter, ice cream, eggs and cheese slices. In an action for infringement and passing off the plaintiff sought an order to amend the defendant's registration by striking out therefrom the words "Royal" or "Royal Gold". The defendant counterclaimed for an order striking out the plaintiff's registration of the word "Royal" for use in association with ice cream. *Held:* That having regard to the considerations mentioned in s. 6 of the *Trade Marks Act*, and the principles set out in *British Drug Houses Ltd. v. Battle Pharmaceuticals*, [1944] Ex. C.R. 239 (affirmed [1946] S.C.R.

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50), the defendant's mark "Royal Gold" is not confusing with the plaintiff's mark "Royal" within the meaning of the *Trade Marks Act* and does not infringe any right flowing from its registration. 2. That since the evidence disclosed no act or conduct on the part of the defendant contrary to the prohibitions contained in s. 7 of the *Trade Marks Act*, the claim for passing off fails. 3. That as applied to goods the word "royal" is not a common laudatory epithet, nor is it "clearly descriptive or misdescriptive" of the quality of goods so as to fall within the prohibition of s. 26(1)(*f*) of the *Unfair Competition Act*. 4. That the mark "Royal" was not "similar" withing the meaning of the *Unfair Competition Act* to "Royal Purple", "Royal Oxford", "Royal African", "Mount Royal", "Royal Canadian" or "Royal Scarlet", which were already on the register in respect of some of the same or similar wares at the time of the plaintiff's registration was not objectionable on that ground. 5. That, in seeking expungement of the plaintiff's registration under s. 18(1)(*b*) of the *Trade Marks Act*, the onus was on the defendant to show that at the time of the commencement of the proceedings the plaintiff's mark "Royal" was not distinctive and, as this onus has not been discharged, the defendant's claim failed. *Great Tower Street Tea Co. v. Smith*, 6 R.P.C. 165; *Coca-Cola Co. of Canada v. Pepsi-Cola Co. of Canada*, [1940] S.C.R. 17; *R. DeMuths Application*, 44 R.P.C. 27, distinguished. CHARLES YEATES & CO. LTD. v. INDEPENDENT GROCERS' ALLIANCE DISTRIBUTING CO. LTD.....36

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WATER CARRIAGE OF GOODS ACT, 1936, R.S.C. 1952, c. 291.
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WHETHER PAYMENTS TAXABLE.
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WHETHER PROFIT ON PART PURCHASED FOR INVESTMENT SUBJECT TO TAX.
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WHETHER "ROYAL" A "COMMON LAUDATORY EPITHET" OR "CLEARLY DESCRIPTIVE OR MISDESCRIPTIVE" WORD MARK
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WHETHER SUM REFERRED TO AS "INTEREST", CAPITAL OR INCOME.
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WHETHER TAX EXEMPT AS A CHARITABLE OR NON-PROFIT ORGANIZATION.
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WHETHER TRADE MARKS "ROYAL GOLD" AND "ROYAL" CONFUSING.
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