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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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.

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.