
BETWEEN:

ATLANTIC SUGAR REFINERIES LIMITED ..... } APPELLANT;

AND

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

1945
Apr. 2
1948
Oct. 26

Revenue—Income Tax—Income War Tax Act, R.S.C. 1927, c. 97, s. 3—Profit on isolated transaction outside ordinary course of business—Speculative investment—Operation of business in a scheme for profit making.

Appellant was faced with a prospective loss in its ordinary business operations through having bought raw sugar at high prices and undertaken to sell refined sugar at existing prices. To recoup such operating loss and in the belief that the prices of raw sugar were too high it sold raw sugar for future delivery on the New York Coffee and Sugar Exchange and later bought raw sugar for future delivery. On these transactions appellant made a profit on which it was sought to hold it liable to income tax.

Held: That the appellant's transactions in the raw sugar futures market were not an investment in raw sugar or otherwise of a capital nature. *McKinlay* v. *H. T. Jenkins and Son, Limited* (1926) 10 T.C. 372 distinguished

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

3. That the appellant's venture into the raw sugar futures market was not unconnected with its business but closely connected therewith.

4. That the profit of the appellant from its sales and purchases in the raw sugar futures market may fairly be regarded as "a gain made in an operation of business in carrying out a scheme for profit making", or "a profit made in the operation of the appellant company's business". *Californian Copper Syndicate* v. *Harris* (1904) 5 T.C. 159 and *T. Beynon and Co., Limited* v. *Ogg* (1918) 7 T.C. 125 followed.

APPEAL under the Income War Tax Act.

The appeal was heard before the Honourable Mr. Justice Thorson, President of the Court, at Ottawa.

Hon. S. A. Haydon K.C. for appellant.

R. Forsyth K.C. and *A. A. McGrory* for respondent.

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

The PRESIDENT now (October 26, 1948) delivered the following judgment:

This appeal is from the income tax assessment levied against the appellant for the year 1939, to the extent that it was thereby sought to hold it liable to tax on the profit made by it in such year from sales and purchases of raw sugar on the New York Coffee and Sugar Exchange.

The facts are not in dispute. Mr. E. S. Johnston, the treasurer of the appellant, filed a statement giving particulars of the said sales and purchases during September and October, 1939. They were contracts for the sale and purchase of raw sugar for future delivery made in the terms of a contract known on the Exchange as Raw Sugar Contract No. 4. The contracts so made were commonly described with reference to the months of delivery specified therein as, for example, December No. 4 Contracts, March No. 4 Contracts, etc. The sales and purchases were in lots of 50 tons each. The appellant dealt through two brokers. Through one of them its sales of raw sugar were as follows: on December No. 4 contracts 20 lots

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on September 11, on March No. 4 contracts 8 lots on September 11 and on May No. 4 contracts 30 lots on various dates from September 11 to October 9.

Subsequently, through the same agent it purchased raw sugar for delivery in the months of delivery of its sales, in amounts equal to those of its sales, as follows: on December No. 4 contracts 20 lots on various dates from September 19 to October 27, on March No. 4 contracts 8 lots on October 27 and on May No. 4 contracts 30 lots on October 27. On the sales and purchases made through this agent the appellant made a profit of $33,201.31. Through the other broker it sold on May No. 4 contracts 40 lots on September 11, and purchased on May No. 4 contracts 40 lots on October 23 and October 27. On these transactions it made a profit of $30,927.60. These two amounts were in New York funds which meant an additional 11 per cent in Canadian funds, making a total profit on its raw sugar contracts in Canadian funds of $71,183.09.

These sales and purchases in the raw sugar futures market were made at the instance of the appellant's president and general manager, Mr. L. Seidensticker, and subsequently approved by its directors. Mr. Seidensticker outlined the events that led up to the transactions and explained his reasons for making them. Immediately after the outbreak of the war at the beginning of September, 1939, there was a heavy demand for sugar by the consuming public and industrial users whereupon the Canadian sugar refining and beet sugar industries were called to Ottawa to meet a committee of control set up by the Canadian government, which requested them to meet the heavy demand without any increase in price. This was prior to the establishment of price controls and rationing. The industries, including the appellant, undertook to sell all the sugar they had at existing prices and went into the cash market to buy raw sugar the prices of which were rapidly advancing. For example, the appellant, because of the drain on its raw sugar supplies to meet the heavy demands for sugar, purchased in September 15,515 tons of raw sugar in the cash market for future delivery, at prices substantially above those previously paid. Subsequently, the authorities found that more stringent measures were necessary and instituted sugar control and appointed

a Sugar Controller. Thereafter, the Sugar Controller was the sole source of supply of raw sugar for the Canadian sugar refining industry and the price of refined sugar was fixed. But this, of course, did not affect the commitments for the purchase of raw sugar at high prices which the appellant had already made.

Mr. Seidensticker explained that in the interval before the establishment of sugar control the necessity of the appellant responding to the demand to supply sugar and the need of buying raw sugar to overcome the deficiencies which normally and naturally occurred resulted in his attempt to recoup what he feared might be a consequent loss resulting from the purchases of raw sugar at high prices, which would, of course, be an operating loss. His attempt took the form of the sales and purchases referred to. He put his reasons for venturing into the futures market in various ways, all of the same tenor; he thought perhaps that something in the market might be found to provide a speculative offset to the appellant's operating loss and he conferred with a friend of his in New York and on his advice and working in conjunction with him entered into the transactions on the New York Coffee and Sugar Exchange; they were entered into for the purpose of offsetting the loss referred to; it seemed to him that to a limited degree the market offered the possibility of a profit on the short side if raw sugar was sold to recoup the appellant for the anticipated loss on the high priced sugar it had bought; it was a speculative transaction to recoup its losses; he thought that there was a good probability of a speculative gain in the futures market; he thought that the price in the futures market on September 11 was so high that it offered possibilities of a gain or profit to the company and would recoup it for the loss it had sustained through the purchase of sugars at high prices; the venture into the raw sugar futures market was made in order to recoup the prospective loss which the appellant was facing.

There are some other facts to which reference should be made. The appellant had power under its letters patent of incorporation

(a) To buy, sell or otherwise deal in, import, export, manufacture, refine, clarify and otherwise prepare for market, sugar, syrup, molasses and all products thereof, and all articles of commerce of a similar nature.

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But while its sales and purchases of raw sugar on the New York Coffee and Sugar Exchange were thus within its powers it is clear that its ordinary business consisted of purchasing raw sugar, refining it and selling the refined product. It was from these activities that it ordinarily earned its income. It obtained its supplies of raw sugar from many places, but mostly from Cuba and the British West Indies. While it made its purchases of raw sugar for future delivery it did not ordinarily do so on the futures market but through agents or brokers who were direct representatives of holders of actual sugar. It sold its refined sugar direct to customers without the intervention of any exchange. In the ordinary course of its business it did not sell raw sugar at all. Only twice in its history did it venture into the raw sugar futures market, once in March and April, 1937, and again in September and October, 1939. In 1937 it made a small profit of $212.10 which it treated as an item of profit and gain in its ordinary earnings for that year. But in 1939 it recorded its transactions in the futures market in a private journal and did not include its profits in its profit and loss accounts. Mr. Seidensticker denied that the transactions could be regarded as hedging. He claimed that they were quite outside the ordinary business of the appellant and described the venture as "just a gamble or speculation". But on his cross-examination he said that speculating with the appellant's money in a transaction on the futures market was within his authority; while he had no authority to gamble in such things as oil wells he did have authority to gamble in sugar futures.

When the assessment for 1939 was made the profits of the appellant from its "operations on raw sugar futures" amounting to $71,183.09 were added to the amounts of income shown on the appellant's income tax return. From such assessment an appeal was taken to the Minister who confirmed it on the ground that the appellant's profit from its raw sugar futures operations was income within the meaning of the Act. Being dissatisfied with the Minister's decision the appellant now brings its appeal from the assessment to this Court.

The issue on the appeal is whether the profit of the appellant on its dealings in raw sugar was taxable income

within the meaning of the Income War Tax Act, R.S.C. 1927, chap. 97, section 3 of which defined taxable income as follows:

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

The argument of counsel for the appellant may be summarized briefly. His first submission was that the amount of the appellant's gain from its transactions in the raw sugar futures market was a capital gain; that it was made such by the employment of its capital for purposes other than its usual business operations; that the transactions were a speculative investment in the raw sugar futures market; and that they were the same as if the appellant had purchased shares of a mining or industrial company or foreign exchange and made a profit thereon. The other submission, really the converse of the first one, was that the gain was not taxable income within the meaning of section 3 of the Act, because it was not income from any trade which the appellant carried on and because the transactions were not part of the normal business operations of the appellant or necessarily incidental thereto but isolated transactions. It was urged that the question of what constituted the appellant's business was a question of fact to be determined not by what it had power under its charter to do but by what it actually did; that its ordinary business was not that of buying and selling raw sugar, but of buying raw sugar for the purpose of refining it, refining such sugar and selling the refined sugar and that it was taxable only on the annual net profit or gain from such business; that it was no part of its business operations to speculate in the raw sugar futures market; that the fact that its transactions there were dealings in raw sugar and it was part of its business to purchase raw

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sugar to refine it should not make any difference, for while it could purchase its raw sugar requirements in the futures market that was not its usual and ordinary manner of acquiring its raw sugar supplies, and it did not sell raw sugar as a matter of ordinary and usual practice; that its venture into the raw sugar futures market was unusual and outside the ordinary course of its operations; and that its transactions there constituted an isolated transaction quite apart from its business so that its gain therefrom was not taxable income. Counsel also argued that if the appellant had made a loss on its raw sugar futures transactions it could not have deducted such loss as an expense for it would not have been wholly, exclusively and necessarily laid out for the purpose of earning the appellant's income.

In support of his submissions that the appellant's gain from its transactions in the raw sugar futures market was a capital gain and not taxable income counsel relied upon *McKinlay* v. *H. T. Jenkins and Son, Limited* (1), sometimes referred to as the *Marble* case, and contended that it was applicable to the present case. There the Company carrying on the business of marble, granite and stone merchants at Torquay, England, had made a contract to supply a quantity of marble for use in a building in Shanghai. Anticipating that it would be necessary to buy the marble in Italy the Company bought Italian lira in March, 1921, although the marble did not have to be obtained until six months later. The lira were bought at 103 to the pound. By May they had risen in value to 72 to the pound and the Company decided to sell them. It did so and realized a profit of £6,707 thereby. Later, when the time came to buy the Italian marble to be supplied under the contract it had to buy lira again. The Special Commissioners held that the £6,707 profit made on the sale of the lira was not a profit assessable to income tax and on appeal to the High Court their view was sustained. It was held by Rowlatt J. that the sum was not a profit arising out of the contract for the supply of the marble, but merely an appreciation of a temporary investment and not assessable to income tax as part of the profits of the Company in the way of its business as a profit of its

(1) (1926) 10 T.C. 372.

trade. The case has been the subject of judicial comment. It was distinguished in *Commissioners of Inland Revenue* v. *George Thompson & Co., Ltd.* (1). There the Company, which carried on business as ship owners, merchants, ship brokers, freight contractors and carriers, had entered into a contract for the supply to it of coal. Subsequently, some of its ships were requisitioned by the Australian government with the result that it had a surplus of coal to be delivered to it for which it had no immediate use. It transferred the benefits under its coal contract to a third party at a profit. Although the Company had power to deal in coal it did not make a practice of selling coal. Rowlatt J. held that the coal transactions were on revenue account and that the profits therefrom were part of the Company's profits. At page 1102, he referred to his decision in the *Marble* case (*supra*) as follows:

> there the way I looked at it . . . was simply this, that they had some capital lying idle, and they embarked upon an exchange speculation. They bought the lire as a speculation, not as consumable stores, or anything of that sort, but they simply bought them as a speculation rather than keep the money in the bank.

It is thus clear that he regarded the purchase of the lira in advance of its being required as a speculation in exchange unconnected with the Company's business as marble merchants. This explanation of the decision in the *Marble* case (*supra*) was adopted in *Imperial Tobacco Co.* v. *Kelly* (2). There the appellants were tobacco manufacturers who were in the habit of buying large quantities of tobacco leaf for cash in the United States. In order to make these purchases it was necessary for them to acquire dollars and they had accumulated dollars for such purpose. On September 9, 1939, the British Treasury requested them to stop all further purchases of tobacco leaf and they did so. This left them with a large surplus of dollars. On September 30, 1939, they were required under the Defence (Finance) Regulations to sell the surplus dollars to the Treasury. They had risen in value, with the result that the appellants had a large profit. They contended that although the dollars were bought for the purpose of their trade they ought to be regarded as having been purchased for the purpose of making a "temporary

(1) (1927) 12 T.C. 1091.

(2) (1943) 1 All E.R. 431; (1943) 2 All E.R. 119.

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investment in foreign currency" and as having, therefore, no connection with their trade and the decision of Rowlatt J. in the *Marble* case (*supra*) was relied upon. The Special Commissioners, however, held that the profits made by them on the compulsory sale of the surplus dollars to the British Treasury must be included in the computation of the profits of their trade. Their view was sustained in the Court of King's Bench by Macnaghten J., whose judgment was affirmed by the Court of Appeal, which refused leave to appeal to the House of Lords. My reading of the decisions in the *Imperial Tobacco Co.* case (*supra*) leads me to think that neither Macnaghten J. nor Lord Greene M.R. considered the *Marble* case (*supra*) wholly free from doubt. But, whether that is so or not, I am unable to see how the appellant's transactions in raw sugar futures can be brought within the ambit of the principle of the *Marble* case (*supra*), even on the basis of the view taken by Rowlatt J. that the Company bought the lira as a speculation unconnected with its business. The only thing in common between the transactions in that case and the appellant's transactions in this one is the element of speculation. That is not sufficient to determine whether a transaction is of a capital or a revenue nature. There are many transactions of a speculative nature that are nevertheless trading or business operations the profits from which are assessable to income tax. The appellant's speculation in the raw sugar futures market was of quite a different nature from that described by Rowlatt J. in the *Marble* case (*supra*). It was not a case of idle capital being temporarily invested in sugar. I think it is fanciful to say that the appellant was making a temporary investment in raw sugar and that such investment stood in the same position as if it had purchased shares of a mining or industrial concern or foreign exchange for a purpose unconnected with its business. There was, in my view, nothing of a capital or investment nature in the appellant's transactions.

There remains the contention that the appellant's gain was not taxable income because it was not income from any trade and because its venture was an isolated transaction outside its normal business operations and unconnected therewith. The appellant cannot escape liability

merely by showing that its entry into the raw sugar futures market was an isolated transaction. While it is recognized that as a general rule an isolated transaction of purchase and sale outside the course of the taxpayer's ordinary business does not constitute the carrying on of a trade or business so as to render the profit therefrom liable to income tax—*vide Commissioners of Inland Revenue* v. *Livingston et al* (1); *Leeming* v. *Jones* (2); it is also established that the fact that a transaction is an isolated one does not exclude it from the category of trading or business transactions of such a nature as to attract income tax to the profit therefrom. There are numerous expressions of opinion to that effect—*vide Californian Copper Syndicate* v. *Harris* (3); *T. Beynon and Co., Limited* v. *Ogg* (4); *McKinlay* v. *H. T. Jenkins and Son, Limited* (5); *Martin* v. *Lowry* (6); *The Cape Brandy Syndicate* v. *Commissioners of Inland Revenue* (7); *Commissioners of Inland Revenue* v. *Livingston* (8); *Balgownie Land Trust, Ltd.* v. *Commissioners of Inland Revenue* (9); and *Anderson Logging Co.* v. *The King* (10).

Whether the gain or profit from a particular transaction is an item of taxable income cannot, therefore, be determined solely by whether the transaction was an isolated one or not. A further test must be applied. One such test was laid down in *Californian Copper Syndicate* v. *Harris* (11). There a company was formed to acquire and re-sell mining properties. After acquiring and working a certain property it sold it at a profit. It was held that such profit was assessable to income tax. At page 165, the Lord Justice Clerk (Macdonald) said:

> 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 realize it, and obtains a greater price for it than he originally acquired it at, the enhanced price is not profit in the sense of Schedule D of the Income Tax Act of 1842 assessable to Income Tax. But it is equally well established that enhanced values obtained from

(1) (1926) 11 T.C. 538 at 543, per Lord Sands
(2) (1930) 1 K.B. 279; (1930) A.C. 415.
(3) (1904) 5 T.C. 159.
(4) (1918) 7 T.C. 125 at 133.
(5) (1926) 10 T.C. 372 at 404.
(6) (1925) 11 T.C. 297 at 308, (1926) 1 K.B. 550 at 554, (1927) A.C. 312.
(7) (1920) 12 T.C. 358.
(8) (1926) 11 T.C. 538.
(9) (1929) 14 T.C. 684 at 691.
(10) (1925) S.C.R. 45 at 56.
(11) (1904) 5 T.C. 159.

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realization or conversion of securities may be so assessable, where what is done is not merely a realization or change of investment, but an Act done in what is truly the carrying on, or carrying out, of a business . . .

What is the line which separates the two classes of cases may be difficult to define, and each case must be considered according to its facts; the question to be determined being—Is the sum of gain that has been made a mere enhancement of value by realizing a security, or is it a gain made in an operation of business in carrying out a scheme for profit making.

The Court came to the conclusion that the sale of the property in question was a proper trading transaction. The statement of principle by the Lord Justice Clerk in the *Californian Copper Syndicate* case (*supra*) has been approved by Lord Dunedin, speaking for the Judicial Committee of the Privy Council, in *Commissioner of Taxes* v. *Melbourne Trust, Limited* (1); by Lord Buckmaster in the House of Lords in *Ducker* v. *Rees Roturbo Development Syndicate, Limited* and *Commissioners of Inland Revenue* v. *Rees Roturbo Development Syndicate, Limited* (2); and by Duff J., as he then was, speaking for the Supreme Court of Canada, in *Anderson Logging Co.* v. *The King* (3), which judgment was affirmed by the Judicial Committee of the Privy Council (4).

The test to be applied was put in a somewhat narrower form in *T. Beynon and Co., Limited* v. *Ogg* (5). There a company carrying on business as coal merchants, ship and insurance brokers and as sole selling agents for various colliery companies, in which latter capacity it purchased waggons for its clients, made a purchase of waggons on its own account as a speculation and subsequently sold them at a profit. It contended that since the transaction was an isolated one the profit was in the nature of a capital profit on the sale of an investment and should be excluded in computing its liability to income tax. But it was held that it was made in the operation of the Company's business and properly included in the computation of its profits therefrom. Sankey J. put the matter thus, at page 132:

> The only question one has to determine is which side of the line this transaction falls on. Is it . . . in the nature of capital profit on the sale of an investment? Or is it . . . a profit made in the operation of the Appellant Company's business?

(1) (1914) A.C. 1001 at 1010.
(2) (1928) A.C. 132 at 140.
(3) (1925) S.C.R. 45 at 48.
(4) (1926) A.C. 140.
(5) (1918) 7 T.C. 125.

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The test thus put is really to the same effect as that laid down by the Lord Justice Clerk in the *Californian Copper Syndicate* case (*supra*). Certainly it was so regarded by Duff J. in *Anderson Logging Co.* v. *The King* (1).

A more specific test was suggested in *Commissioners of Inland Revenue* v. *Livingston* (2). There the respondents, a ship repairer, a blacksmith and a fish salesmen's employee, purchased as a joint venture a cargo vessel with a view to converting it into a steam-drifter and selling it. They were not connected in business and had never previously bought a ship. Extensive repairs and alterations to the ship were carried out and then respondents sold the vessel at a profit. It was held that they were assessable to income tax in respect of it. At page 542, the Lord President (Clyde) said:

> I think the test, which must be used to determine whether a venture such as we are now considering is, or is not, "in the nature of trade", is whether the operations involved in it are of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made. If they are, I do not see why the venture should not be regarded as "in the nature of trade," merely because it was a single venture which took only three months to complete.

This statement of the test to be applied was approved by Rowlatt J. in *Leeming* v. *Jones* (3). He regarded it as covering all the cases.

While it may not be possible to define the line between the class of cases of isolated transactions the profits from which are not assessable to income tax and that of those from which the profits are so assessable more precisely than in the tests referred to, it is clear that the decision cannot be made apart from the facts. The character or nature of the transaction must be viewed in the light of the circumstances under which it was embarked upon and the decision as to the side of the line on which it falls made after careful consideration of its surrounding facts.

While there are cases in which it is difficult to decide on which side of the line a transaction falls, I find no such difficulty in the present case. In my opinion, Mr. Seidensticker's evidence is a complete answer to the appellant's contentions. He said of its transactions in the raw sugar futures market: "I think it is difficult to disassociate them

(1) (1925) S C.R. 45 at 49
(2) (1926) 11 T.C. 538.
(3) (1930) 1 K.B. 279 at 283.

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from what took place in the first instance." In my view, it is impossible to do so. It is clear from his evidence that the appellant entered into the transactions because it had been caught in an abnormal situation in its business operations in its ordinary field and thought it could offset the consequences thereof, to some extent at least, by operating in a related field. It was faced with a prospective loss because of its purchases of raw sugar at high prices and its undertaking to sell refined sugar without any increase in price and with the likelihood of sugar control and a fixed price. There seemed no possibility of avoiding such loss if it confined its business operations to their usual and ordinary course. This was the abnormal emergency situation in the appellant's business that led Mr. Seidensticker to the venture in the raw sugar futures market. With his knowledge of the sugar business and sugar prices and the advice of his friend in New York he thought that the prices of raw sugar were too high and would fall. It was only in such a free market as the raw sugar futures market in New York that he could put his knowledge and judgment to profitable use. The venture into such market was thus not an isolated transaction that was unconnected with the appellant's business. On the contrary it was closely connected therewith. It was impossible to listen to Mr. Seidensticker without being constantly reminded of this close connection. That theme ran through the whole course of his evidence. Emergency situations in business frequently beget departures from the usual and ordinary course without any change in the character of such departures as business transactions. That is what happened in the present case. It was the abnormal situation in the appellant's business in its ordinary course that took it into the raw sugar futures market. It was only because of its prospective loss through its purchases of raw sugar at high prices in the cash market that it decided to sell and subsequently purchase raw sugar in the futures market. The sales and purchases in the futures market would not have happened otherwise; they were, in a sense, the result of what had happened in its ordinary course of business. Moreover, quite apart from their cause, they were transactions in the same commodity as that which it had to purchase for its ordinary purposes. In my view,

they were of the same character and nature as trading and business operations as those of its business in its ordinary course, even although they involved a departure from such course. The appellant made such departure an operation of its business.

Under all the circumstances, I am unable to see how the transactions can be regarded as an investment in raw sugar or as otherwise of a capital nature. In my judgment, the profit of the appellant from its sales and purchases in the raw sugar futures market may fairly be regarded as "a gain made in an operation of business in carrying out a scheme for profit making", or "a profit made in the operation of the appellant company's business." The operations involved in the transactions were also "of the same kind, and carried on in the same way, as those which are characteristic of ordinary trading in the line of business in which the venture was made."

That being so, the appellant has failed to show error in the assessment appealed from. Its profit from its transactions in the raw sugar futures market was properly included as an item of taxable income in its hands. The appeal must, therefore, be dismissed with costs.

Judgment accordingly.