BETWEEN:

RIVERSHORE INVESTMENTS LIMITED ..... APPELLANT;

1962
Oct. 18
1964
Feb. 27

AND

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

Revenue—Income tax—Income Tax Act, R.S.C. 1952, c. 148, s. 137(1)—Artificial transaction—Sale and repurchase of land—Intention of company deemed to be that of its directors—Directors profiting personally from transaction.

Leslie Farkas and Andrew Gaty, who were active as individuals in the real estate business, owned all the shares of Crosstown Realties (Mtl) Inc and ⅔ of the shares of the appellant company, and between them, held the positions of president and secretary of both companies. In April 1955, the two men offered to purchase a parcel of land in the County of Laprairie, Quebec, for $32,500, the deal being completed on June 30, 1955 with the property being conveyed to the appellant at their direction On July 6, 1955, one Leslie Benko made an offer through Crosstown Realties (Mtl) Inc to purchase the said land for $35,000 On September 14, 1955, before obtaining title to the said land, Benko offered to sell it through Crosstown Realties (Mtl) Inc. to its nominee for $61,000. On September 30, 1955, Benko secured title to the said land and on the same date he reconveyed it to the appellant. On the next day, October 1, 1955, Benko received a cheque for $26,000 issued by the appellant and signed by Gaty as president, ostensibly in payment of the difference between the price Benko had agreed to pay for the land and the price for which the appellant had agreed to repurchase it from him. The appellant resold the said land to River Construction Limited on October 30, 1955 for $65,000. There was no evidence that either Benko's offer of July 6 to purchase the said land from the appellant, or his offer of September 14 to sell it back to the appellant had ever been accepted or that the deposits stipulated for in both offers had ever been paid. In addition, Crosstown Realties (Mtl) Inc. did not charge a commission in respect of either transaction.

Subsequent to October 1, 1955, Benko endorsed the cheque for $26,000 and gave it to Farkas and Gaty as payment for 2,600 non-cumulative, 4% non-participating, non-voting preference shares in Crosstown Realties (Mtl) Inc. with a par value of $10 per share, which were owned by Farkas and Gaty and which were not transferable without their consent. The evidence established that the shares had only a nuisance value of about $1.00 per share in the hands of Benko.

Held: That the repurchase of the land by the appellant for $26,000 more than it had sold it to Benko for, constituted a clever but artificial scheme whereby Farkas and Gaty succeeded in realizing a handsome profit personally on the sale of the 2,600 preference shares in Crosstown Realties (Mtl) Inc., and this with money provided by the appellant and but for which the said $26,000 would have been included in the appellant's taxable income.

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2. That the intentions of the appellant are deemed to be those of its directors and it is bound by the artificiality of the transactions carried out by its directors.

3. Appeal dismissed.

APPEAL under the *Income Tax Act*.

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

R. E. Parsons for appellant.

Paul Boivin, Q.C. and *Sydney Phillips* for respondent.

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

KEARNEY J. now (February 27, 1964) delivered the following judgment:

This is an appeal from a notice of reassessment whereby the Minister added to the appellant's taxable income otherwise payable for its taxation year ended June 30, 1956 an amount of $26,000, which the Minister declared was a disbursement or expense made or incurred by the taxpayer which was designed to artificially reduce its taxable income for the said year, as contemplated in s. 137(1) of the *Income Tax Act*, R.S.C. 1952, c. 148 (as amended), and which reads as follows:

> In computing income for the purpose of this Act, no deduction may be made in respect of a disbursement or expense made or incurred in respect of a transaction or operation that, if allowed, would unduly or artificially reduce the income

The evidence in the case consisted of the testimony of four witnesses, Messrs. Leslie Farkas and Andrew Gaty, who were called at the instance of the appellant, and Mr. Leslie Benko and Mr. P. Gould, C.A., who were heard on behalf of the respondent, together with various exhibits filed by them, as well as the documents transmitted by the Minister pursuant to s. 100(2) of the Act.

Apart from Mr. Gould, who gave expert evidence as to the value of certain shares of stock—later described—, the other three witnesses were personally interested in the transactions in issue.

It is common ground that the aforesaid reassessment arises out of certain transactions nearly all of which are in

documentary form and which were all concerned with the same piece of real estate, composed of about twenty arpents, situated in the County of Laprairie, in the Province of Quebec (hereinafter sometimes referred to as "the property").

I propose to summarize the documentary evidence supplemented by reference to some verbal evidence which has not been disputed and which may serve to make the documents more readily understandable.

Messrs. Farkas and Gaty were engaged in the real estate business in Montreal and operated through three media, namely, by acting in their personal capacity, through the appellant company, of which they were secretary and president respectively and owned between them two-thirds of its capital-stock, and the third medium was Crosstown Realties (Mtl) Inc. which was engaged in a real estate agency business and its entire issued stock was owned by Messrs. Farkas and Gaty (or members of their families); they were its president and secretary respectively. Mr. Benko was in no way related to them nor did he hold any stock in either of the above companies prior to October 1, 1955.

The following is a brief summary of the documentary evidence of the foregoing transactions, some of which I will comment upon more fully later.

In April 1955 Messrs. Farkas and Gaty made an offer to purchase the property from its then owner J. P. Martin for the sum of $32,500 and the deed of sale completing the transactions was to be finalized by June 30, 1955. Messrs. Farkas and Gaty hoped to sell the property prior to the aforesaid date but no buyer could be found. See notice of objection dated October 3, 1958, signed by Andrew Gaty, contained in the documents transmitted by the Minister.

On June 30, as alleged in the statement of facts and admitted in the respondent's reply, Farkas and Gaty caused the appellant company to acquire the property in their stead by a notarial deed dated June 30, 1955 (Ex. P-1), as alleged in paragraph 1 of the statement of facts, which is admitted.

As appears by Exhibit P-2, on July 6, 1955 Leslie Benko made an offer through Crosstown Realties (Mtl) Inc. to pur-

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chase the property for a price of $35,000. The main provisions of the offer are as follows:

6th July, 1955

To CROSSTOWN REALTIES (MTL) INC.
630 Dorchester West
Montreal, P.Q.

Dear Sirs:

I the undersigned hereby offer to Purchase through your agency for myself or for my nominee(s) a piece of land known as P 1-4 in the Parish of Lapraire, having a total surface area of 20.57 arpents english measure and more or less, all as shown on the surveyor's plan prepared by Mr. Lapointe, surveyor, dated 24th May, 1955; The total purchase price to be $35,000 (THIRTY-FIVE THOUSAND DOLLARS) payable as follows and under the following terms and conditions:

1.) $18,750 in cash upon signing of the deed of sale.

2.) $16,250 by assuming the existing first mortgage, bearing interest at the rate of 5% per annum, repayable within five years, all in accordance with the terms and conditions stipulated in the deed creating said mortgage.

* * *

5.) This offer is open for acceptance until the 10th day of July 1955 6 P.M. after which date it becomes nil and void. Herewith my cheque of $2,000 as a deposit on account of the purchase price. This offer can be accepted directly to your company as agents.

—L. BENKO

On September 14, 1955, prior to obtaining title to it, Mr. Benko offered to sell the property through Crosstown Realties to its nominee for $61,000 (Exhibit P-3); the main provisions of the offer are as follows:

14th Sept. 1955

To Crosstown Realties (Mtl) Inc.
630 Dorchester West
Montreal, P.Q.

Dear Sirs:

I the undersigned hereby offer to sell through your agency to your nominee(s) a piece of land known as P 1-4 in the Parish of Lapraire, measuring 20 57 arpents english measure and more or less, all as shown on the surveyor's plan prepared by Mr. Pierre Lapointe surveyor, dated 24th May, 1955. The total sales price to be $61,000 payable as follows and under the following terms and conditions:

1.) $44,750 in cash upon signing of the deed of sale.

2.) $16,250 by assuming the existing first mortgage bearing interest at the rate of 5% per annum, becoming due within 5 years (1960), all in accordance with the terms and conditions stipulated in the deed of sale creating said mortgage.

* * *

5.) This Offer to Sell is open for acceptance until the 18th day of (month missing, should be September) 1955 12 P.M. after which

date it becomes nil and void. If accepted it must be accompanied by a cheque of $2,000 made to my order as a deposit on account of the purchase price.

—L. BENKO

On September 30, 1955 Mr. Benko secured title to the property from the appellant for $35,000 (Ex. P-4) and on the same date he sold it back to the appellant for $61,000 (Ex. P-5), whereupon the appellant acquired immediate title and possession.

On the day following the sale, namely, October 1, 1955, the appellant issued a cheque amounting to $26,000, signed by Andrew Gaty as president of the appellant and payable to the order of Leslie Benko. As appears by the said cheque, it was endorsed by L. Benko and L. Farkas and was cleared for payment on November 3, 1955. The significance of the said cheque endorsement is not explained by any documentary evidence but will be presently disclosed in a review of the testimony of the main witnesses.

As appears by paragraph 4 of the appellant's statement of facts, on October 31 the appellant sold the property to River Construction Limited for $65,000. The deed was not produced, as the said paragraph 4 was admitted in the respondent's reply.

The dispute concerns the artificiality or otherwise of all or any of the transactions described in Exhibits P-3 to P-6 inclusive.

Now, with respect to the testimony of witnesses, apart from his evidence previously referred to and which is non-controversial, Mr. Farkas testified that some time prior to the Benko offer of September 14 (Ex. P-3) he and the latter after discussion agreed that the resale price would be $61,000. In describing what took place when Exhibits P-4 and P-5 were executed Mr. Farkas said that the $61,000 mentioned in the deed was paid to Mr. Benko, and when asked how it was paid he said, "It was an accounting, because, on the same day, Mr. Benko had purchased from the same Corporation the same piece of property for $35,000 and for the difference of $26,000 the appellant company issued a cheque to Mr. Benko", who used it to purchase $26,000 worth of shares from Mr. Gaty and himself.

In cross-examination the witness testified that some time prior to the signing of the Benko offer of September 14 (Ex. P-3) the latter had agreed to accept 2,600 preferred

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shares of Crosstown Realties stock in full settlement of the balance owing him of $26,000. Mr. Farkas also testified that the endorsement of the cheque and the delivery of the shares took place the day after Exhibits P-4 and P-5 had been executed. The witness stated that he eventually cashed the cheque.

Mr. Farkas could not remember when the possibility of Mr. Benko acquiring Crosstown Realties' shares arose or whether the latter inquired into the financial status of the said company.

The witness stated that Mr. Benko, some time before he gave the nominee of Crosstown Realties, which was the appellant, the option to repurchase the property, reminded him and Mr. Gaty that the property was worth much more than the $35,000 which he was paying for it, that he wanted a good price for it and that if Mr. Benko had asked him to release him from his offer he would have been glad to do so. It was Mr. Benko, he said also, who suggested the figure of 26,000 (should read "2,600") Crosstown Realties shares and informed the witness that he wished later on to buy some more shares of the said stock.

Mr. Gaty, apart from giving testimony on facts which are not disputed or which were already referred to in Mr. Farkas' testimony, made some further statements which I think are noteworthy.

Crosstown Realties, he thought, drew up the Benko offer to buy the property for $35,000 (Ex. P-2), and, in respect thereof, Crosstown Realties was acting as agent for the appellant. The above-mentioned company also drew up the offer by Mr. Benko to sell the property to the nominee of Crosstown Realties for $61,000 (Ex. P-3) and, in the latter instance, it was acting both for the appellant and Mr. Benko. Asked if Crosstown Realties received any commission in respect of the $61,000 transaction, the witness stated:

> Because river investment was a company which was two-thirds (⅔) controlled by us, we did not deem it necessary to charge commission to ourselves when it came to resale for Mr. Benko. . . . the price agreed was fixed. We probably could have charged—we could have quoted a few thousand dollars more and charged commission but we did not deem it necessary.

Later, in his evidence, when reminded that Crosstown Realties and the appellant were separate companies, and on

again being asked if a commission had been paid, the witness said, "I mean I don't know, I don't remember that. I don't remember that it was not."

The witness, when questioned about one of the by-laws of Crosstown Realties called "By-law No. 12", which, *inter alia*, stipulated that no transfer of shares could be made without the consent of its directors, agreed that it had not, to his knowledge, ever been repealed.

Mr. Gaty also confirmed that the minutes of a meeting of the directors of Crosstown Realties, dated October 1, record that he and Mr. Farkas sold and transferred to Leslie Benko the 2,600 shares previously referred to.

The witness stated that the reason "we"—meaning, I presume, the appellant—"repurchased the property was because we had a chance to resell it later."

He later stated: "When we made the sale to Benko, which was effected on June 30, there were only hopes that houses would be built in the area, but by the end of the summer they had become facts due to the construction which had been carried out in the immediate neighbourhood during the later summer months . . . ", which accounted for the sudden increase in value of the instant property.

Mr. Benko, during his testimony, filed a letter, signed by himself, addressed to the Inspector of Income Tax in Montreal (Ex. R-1) dated June 12, 1958, which together with his testimony set out his version of his dealings with Messrs. Farkas and Gaty.

As appears from the letter, he controls Benmar Realty Investment Corporation which had acquired two income-bearing properties from which he derives his living. He had, in two separate years, by influencing others to follow his example, received what amounted to commissions, which he reported as taxable income, but stated he did not deal on a business level with immovable property, either as a buyer or seller or brokerage agent.

Mr. Benko, in the aforesaid letter, gave the following account of what prompted him to make the offer of July 6 (Ex. P-2). His family, he stated, consists of an only daughter whose husband was working in Montreal for Dominion Engineering Company Limited. Harbouring some doubts early in 1955 about the permanency of his son-in-law's employment and fearing that he might move to Cali-

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fornia, in order to prevent this occurrence, after much thought and visiting many sites, he decided to acquire the instant property for his son-in-law who was fond of sports, with the intention of developing it into a sports centre, including golf driving range, a miniature golf course, tennis and archery courts and such additional like features. He instructed an architect to prepare drawings of the proposed sports centre who made a sketch dated July 15, 1955. He had rented for part of the summer season a cottage at Donnelly Lake. During the latter part of July, the manager (since deceased) of Dominion Engineering Co. Ltd. and his wife visited him and assured him that he need have no concern about the permanency of his son-in-law's employment and that he should give up all thought of establishing an alternative business for him. The witness abandoned his plans for the centre. The letter goes on to say (p. 2, last para.):

> Upon my return from the summer home to Montreal I notified Messrs. Gaty and Farkas that due to altered circumstances I would not be requiring the property and asked if they could locate a buyer to take it off my hands. I myself tried to find a buyer, but without experience in the handling of land, and with no connections in that business, I was unsuccessful. Subsequently Messrs. Gaty and Farkas indicated to me that they were interested to buy the property, and I agreed that for the difference between my buying and selling price I would obtain and accept 2,600 Preferred Shares of Crosstown Realties Limited, having a par value of $10 each.

The witness testified that he first spoke to Messrs. Farkas and Gaty about selling the property for him when he returned from the country, which, he thought, was at the end of July or some time in August.

Asked if at the above time he also discussed the question of acquiring preferred shares in Crosstown Realties, he answered:

> We spoke for this question when I sell this piece of land and we have plus—I buy for this plus, the shares, I take the shares.
>
> Q. When did you discuss this question of taking the shares?
>
> A. I tell you, I want to sell this piece. First alone, I don't find a buyer for this. I don't find a buyer alone and so, I go back to Mr. Farkas and Gaty and tell them: "Look, I am squeezed, now my house is not sold and I have to pay maybe in a short time and I don't have this money free. Sell me this property for me".

At pages 80 and 81 of the transcript, on being cross-examined by counsel for the appellant, Mr. Benko replied:

> M[e] R. E. PARSONS:
>
> Q. You accepted an offer to purchase this property on July 6th or 7th, 1955?

A. Yes.

Q. And then, you went away for the summer?

A. Yes.

Q. When you came back, you said that you no longer had use for this property?

A. No.

Q. Why was that?

A. Because the Manager for Dominion Engineering working with my son-in-law and he invited us and we spoke about it and I told him I had trouble with my son-in-law, two or three friends of his want to go to the States and I have only one son and daughter and I don't want him to go, what kind of a future he has. So, he told me: "There is a very nice future, he has a very good future in engineering. Why don't you want him to go?" I stopped him, he has a future in the factory, he has today, he has a very nice position. I told him: "Look, you cannot go from here, I will sell the property, I am not interested for that."

* * *

Q. Then, if I understood correctly, you went to see Mr. Farkas and Mr. Gaty?

A. Yes.

Q. And then you also agreed with Mr. Farkas and Mr. Gaty, if I understood you correctly, that with the plus or profit, the difference between your purchase price and what they would get for it, you would buy shares of Crosstown Realties from Mr. Farkas and Mr. Gaty, is that correct?

A. Yes.

M° S. PHILLIPS: The testimony is that he would accept shares, not buy shares. That is the testimony by the letter in evidence.

M° R. E. PARSONS:

Q. At the time the deeds were signed, did you receive payment by River Shore Investments? Did you receive a cheque or cash for the difference?

A. I had a cheque, but I endorsed it and I gave it to Mr. Farkas and Mr. Gaty.

There remains the evidence of Pierce Gould, a chartered accountant who testified that in his opinion the fair market value in 1955 of the 2,600 preferred shares in issue in the hands of anybody who, like Leslie Benko, was not a common-shareholder, was not in excess of $1 per share. The witness arrived at this valuation for the following reasons. The shares in question were non-cumulative-4%-non-participating-non-voting shares and formed part of a block of 4,500 shares which had been issued in 1955 to Messrs. Farkas and Gaty in consideration of the transfer from a company called Crosstown Realties of its goodwill to Crosstown

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Realties (Mtl) Inc. The significant part of the above-mentioned goodwill was made up of a contract which existed between the Town of Préville and Crosstown Realties. The balance sheets of Crosstown Realties Inc. for 1955 to 1961, inclusive, showed that the 4,500 preferred shares originally issued to Messrs. Farkas and Gaty were still outstanding, that they were redeemable at par at the option of the directors and on voluntary winding up the holder would be entitled to nothing more than $1 per share; that no dividend had ever been paid on them and that Leslie Benko had never received from the said company any payment of any kind and that, at the date of trial, he still retained possession of them. Mr. Gould also stated that since no evidence to the contrary was presented to him, he assumed that the commission earnings of the company between 1955 and 1959 were such that in the hands of common-shareholders could be worth par. The profit and loss account for 1961 indicated that the company had current assets of $231,000, almost all of which represented loans receivable the character of which the witness had not examined and it had current liabilities of $227,000.

After comparing the quoted market value of preferred shares which were in a comparable status to the instant shares, the witness was of the opinion that, marketwise, they had only a nuisance value, which he placed at $1 per share.

Counsel for the appellant submitted that the respondent had failed to produce any evidence that the original offer to purchase the property signed by Leslie Benko on July 6, 1955 (Ex. P-2), which contained a requirement that a deed of sale be executed on or before October 1 of the current year, was in any way artificial or a transaction not at arm's length or in the ordinary course of business; that the same was true with respect to the subsequent transactions in issue and, consequently, that the appeal should not be maintained.

Moreover, insofar as the 2,600 shares which Mr. Benko received are concerned, since they were not shares of the appellant company this Court was not entitled to inquire into their value.

Similarly, that while it may well be said in another court on another appeal that Messrs. Farkas and Gaty enjoyed a profit on which they may well have to pay tax, this is not pertinent to the instant case, since we are here dealing with

an appeal from a reassessment against the appellant company and there is no evidence that the foregoing transactions were not made at arm's length and in good faith.

In further support of the non-artificiality of the two transactions described in Exhibits P-4 and P-5, counsel for the appellant submitted that as a result of them the appellant realized a profit of $2,500 when it sold the property to Mr. Benko on September 30 and a further sum of $4,000 when it sold it to River Construction Ltd.; that the above-mentioned profits amounting to $6,250 were reported as taxable income and were the only profits made by the appellant on its real estate transactions; that the payment of $26,000 made by the appellant constitutes an amount which it was required to disburse in order to repurchase the property and that its taxable income for the year amounted to $250, as stated in its income tax report, and not $26,250, as claimed in the Minister's reassessment.

It is submitted on behalf of the respondent that Messrs. Farkas and Gaty, with or without the knowledge of Mr. Benko, used him as a vehicle to cause the appellant to pay an unnecessary and artificial price of $26,000 in repurchasing the property, and but for which the said sum would have been added to the appellant's otherwise taxable income for the year; that since there is abundant proof that Mr. Benko was in financial difficulties and unable to make good his offer to purchase it for $35,000 and anxious to have it "taken off his hands" it is unrealistic to regard his offer to sell the property to the appellant at nearly double such amount, the said offer being an apparent artificial transaction. Moreover, it should be disregarded for taxation purposes, as it was used to conceal the fact that the cheque for $26,000 and the proceeds therefrom, signed on behalf of the appellant by Mr. L. Gaty, payable to Leslie Benko, was to be received on the following day by Messrs. Farkas and Gaty and that what Mr. Benko was to receive was 2,600 worthless shares which belonged to the said Farkas and Gaty. Furthermore, that the appellant had acquired the property for $32,500 and ultimately sold it for $65,000 and that its taxable income derived therefrom was $32,500, not $6,250 as reported by the appellant, and that the difference of $26,000 was taxable income instead of a disbursement or expense which if allowed would artificially reduce its income.

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I cannot accept without reservation the submission of counsel for the appellant that the evidence clearly shows that Mr. Benko's original offer to purchase the property dated July 6, 1955 (Ex. P-2) was made in the ordinary course of business—and this is doubly true of a like submission in respect of the subsequent transactions in issue. Neither can I agree with his submission that this Court is not entitled to inquire into the value of the 2,600 shares of Crosstown Realties stock which Mr. Benko received, because they were not owned by the appellant company.

In my opinion, the value of the shares is very relevant to determine the nature of the transactions with which we are concerned, although I agree with counsel for the appellant that the taxability or non-taxability of the profit which Messrs. Farkas and Gaty enjoyed on the sale of the shares is not before this Court. Nevertheless, I consider that the relationship which had been proven to exist between Messrs. Farkas and Gaty and the company indicates that in making a personal profit they were not dealing with the company at arm's length.

Now, with respect to the submission of counsel for the respondent, I am in agreement that, if it is established that Messrs. Farkas and Gaty made use of Mr. Benko as a vehicle to cause the appellant to pay an unnecessary artificial price of $26,000 in repurchasing the property, it is immaterial whether Mr. Benko was aware or unaware of their interest and purpose in doing so.

I will first comment on Mr. Gould's evidence, as it can be dealt with in a few words.

I am satisfied that while the nominal value of the instant 2,600 preferred shares was $26,000 they had, marketwise, only a nuisance value. Mr. Gould, in coming to this conclusion, did not even take into account the restriction on the transferability of the said shares, which, in my opinion, is the most detrimental element affecting their value.

Now, in respect of the three interested witnesses, I find that I can give little credence to some of the testimony given by Messrs. Farkas and Gaty and certain statements made by Mr. Benko leave the latter's evidence open to suspicion and it is difficult to determine the extent to which it can be relied upon.

I cannot credit Mr. Farkas' testimony wherein he stated that Mr. Benko declared that he wanted later on to buy

more than the 2,600 Crosstown Realties shares which he received. Mr. Benko, in his testimony, made no reference to such a statement and since he knew or could easily have ascertained that the said shares had little value, it is unlikely that he would be disposed to place his own money in such a bad investment.

It seems apparent from Mr. Gaty's evidence, wherein he was dealing with commissions, that he would have no compunction about adding a few thousands dollars to the repurchase price of the property, without regard for the consequences insofar as income tax was concerned.

The above-mentioned three witnesses were unable or failed to produce any written evidence of the acceptance of the Benko offer (Ex. P-2) to purchase the property for $35,000 or of the $2,000 which he allegedly paid on account of the purchase price thereof. The same is true with respect to his offer to sell the property for $61,000 and the $2,000 which he supposedly received on account thereof and I consider that such a situation would not have occurred in transactions which are carried out at arm's length.

Counsel for the appellant appeared to base his whole case on the reliability of the testimony of Mr. Benko and I will deal with it in some detail.

I think that Mr. Benko's recital of events which occurred even before July 1955, when he first came in contact with Messrs. Farkas and Gaty, which are uncorroborated, is, to say the least, rather strange. As we have seen by his long explanatory letter Exhibit R-1, he began to have fears, early in 1955, about the permanency of his son-in-law's position with Dominion Engineering Co. Ltd. and because he was contemplating, on that account, going to California. One would expect that his first thought would be to ascertain from the boy's manager how he was faring—I might here remark that, according to Mr. Benko's letter (Ex. R-1), it appears that the manager of Dominion Engineering Co. and his wife came during the latter part of July to visit him at his country cottage, while in his testimony he stated that he and his son-in-law had been invited to visit the manager; in any event, the manager was accessible. Instead, he began searching for a sports centre site which, if and when developed, would only provide his son-in-law with employment for less than six months per annum. Having found the present property, for which Messrs. Farkas and Gaty

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as late as June 30 were unable to find a purchaser, on July 6 he signed an offer (Ex. P-2) to buy it, and, towards the end of the same month, in order to allay his fears, contacted the latter's manager and learned—apparently for the first time—that he was doing exceedingly well and had a bright future with the company, whereupon Mr. Benko promptly decided to get rid of his commitment to purchase the property. It has been said that sometimes "truth is stranger than fiction" and perhaps it may be applicable to his aforesaid early evidence.

Some aspects of his later actions I think, are more open to suspicion. By putting a most favourable construction on such subsequent actions, however, I think, it could be argued that Mr. Benko found himself in the position of being unable to raise the necessary money to make good his offer to purchase the property and I believe it is obvious that his first concern was to obtain a release from his obligation to pay $35,000 for the property. This is borne out by Exhibit P-4 in which there is an acknowledgment that he had discharged his obligation, as appears by Exhibit P-4, which, in part, states:

> THE PRESENT SALE is thus made for and in consideration of the price and sum of THIRTY-FIVE THOUSAND DOLLARS ($35,000), on account and in deduction whereof the Vendor acknowledges to have well and truly received of and from the Purchaser herein, the sum of eighteen thousand seven hundred and fifty dollars ($18,750), and whereof quit for so much

The balance was taken care of by his assumption of the existing mortgage amounting to $16,250. Secondarily, if he were able, without risk, to obtain anything in addition, so much the better. This, in my opinion, explains why, without any writing to evidence it, he agreed to accept, by prearrangement, the aforementioned 2,600 shares without taking the ordinary precautions of inquiring or having someone inquire on his behalf into the financial status and corporate setup and by-laws of Crosstown Realties. If he had done so, he would have perceived how valueless they were, particularly since, due to their non-transferability without the consent of Messrs. Farkas and Gaty, they would be the only prospective buyers of the shares.

In order to attribute the above-mentioned motives to Mr. Benko, I think one must assume that, unlike Messrs. Farkas and Gaty, he was not aware of the construction develop-

ment which by the end of the summer had tremendously increased the value of the property. If he were aware of it, then I cannot believe he would have parted with the $26,000 cheque which he received the next day in exchange for the relatively worthless shares of Crosstown Realties, unless he were serving as an accommodation party under Messrs. Farkas and Gaty. A further indication of the artificiality of the cheque, insofar as Mr. Benko was concerned, is the fact that, in his long explanatory letter Exhibit R-1, he made no reference to it nor what he did with it and it was only long afterwards, in the concluding lines of his testimony, that he stated that he received a cheque, endorsed it and gave it to Messrs. Farkas and Gaty. In any event, as earlier mentioned, insofar as Mr. Benko's evidence is concerned, I agree with the submission of counsel for the respondent that, if it can be established that Messrs. Farkas and Gaty caused the appellant to pay an artificial price amounting to $26,000 in repurchasing the property, it is immaterial whether this was done with or without the knowledge or connivance of Mr. Benko, since it was not he but themselves who obtained the $26,000 paid by the company.

In my opinion an analysis of the evidence of this case clearly discloses that, in respect of the transactions of September 14 (Ex. P-3) and the two transactions which occurred on September 30 (Exhibits P-4 and P-5) and the verbal transaction which took place the day following, the appellant company was not a free agent because its president and secretary, acting in their own personal interests, required the latter company to expend $26,000 more than was necessary to repurchase the property from Mr. Leslie Benko; that the money used to effect the said repurchase constituted a clever but artificial scheme whereby Messrs. Farkas and Gaty succeeded in realizing a handsome profit personally on the sale of the previously mentioned 2,600 preferred shares, and this, with money provided by the appellant and but for which the said $26,000 would have been included in the appellant's taxable income when it sold the property for $65,000 on October 1, 1955.

Dealing with Exhibit P-3, it is clear that quite some time before September 14 Messrs. Farkas and Gaty had procured the consent of Mr. Benko that, for the difference between the purchase price to be fixed for the property and the $35,000 which Mr. Benko was required to pay for it, the

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latter would accept 2,600 shares of preferred stock which he knew (or should have known) had but a nuisance value. I am convinced, notwithstanding any evidence to the contrary, that the so-called discussion between Messrs. Farkas and Gaty and Mr. Benko, as to the fixing of the amount of the repurchase price, was a one-sided affair, that it was determined by Messrs. Farkas and Gaty and agreed to by Mr. Benko, and but for the aforesaid verbal understanding the repurchase price mentioned in Exhibit P-5 would never have been fixed at $61,000.

As we have seen, the evidence establishes that Messrs. Farkas and Gaty desired to repurchase the property because they knew that they had a good chance of disposing of it. As a matter of fact, they did dispose of it within thirty days of repurchase for $65,000.

I think it may be reasonably inferred from the evidence that Messrs. Farkas and Gaty, if they were not fully aware that they would be able to shortly realize $65,000 for the property, they were confident that it would bring at least $61,000, and this explains why they inserted the last-mentioned figure in Exhibit P-5.

The advantage to Messrs. Farkas and Gaty personally of having the purchase price in Exhibit P-5 fixed at $61,000 is obvious, because when the property was later sold for $65,000 the company could deduct $61,000 and report a taxable gain of $4,000. In absence of any proof that they made a business of buying or selling shares, to all appearances they would make a non-taxable capital gain of about $26,000. *Per contra,* the appellant company—which they controlled—would be required to pay practically no income tax at all, since after reporting the $2,500 difference between the $32,500 they originally paid for the property and the $35,000 Mr. Benko allegedly paid for it and the $4,000 of taxable gain realized on the ultimate sale of the property for $65,000, the only taxable income which remained, according to the appellant's income tax return, amounted to $250, whereon the tax payable amounted to $32.50, instead of $26,250 and $5,100 respectively as assessed by the Minister.

A further indication of the artificiality of Exhibit P-5 is, I consider, the fact that it was the day after the said exhibit

had been signed that Mr. Gaty caused the appellant to issue the cheque for $26,000 payable to Mr. L. Benko, dated October 1, 1955 (Ex. P-6), although Mr. Benko had agreed to wipe out $26,000, the difference between $35,000 and $61,000, as set forth in Exhibit P-5:

POSSESSION

By virtue of these presents, the Purchaser shall become the absolute owner of the immoveable hereby sold, with immediate possession thereof.

PRICE

THE PRESENT SALE is thus made for and in consideration of the price and sum of SIXTY-ONE THOUSAND DOLLARS ($61,000), on account and in deduction whereof the Vendor acknowledges to have well and truly received, of and from the Purchaser herein, the sum of forty-four thousand seven hundred and fifty dollars ($44,750), and whereof quit for so much.

AND as to the balance remaining, namely, the sum of sixteen thousand two hundred and fifty dollars ($16,250), the Purchaser hereby binds and obliges itself to pay the same, to the entire exoneration and acquittal of the Vendor, . . .

I do not think that it can be said that the appellant freely consented to pay $26,000 to repurchase a property which Leslie Benko, the vendor, was willing to part with for shares that had little or no market value, particularly when the recipients of the cheque for the said amount were two of its own directors.

I consider, however, that the intentions of the appellant are deemed to be those of its directors and it is bound by the artificiality of the transactions carried out by the said directors. *Vide:* Kerwin J., as he then was, in *Atlantic Sugar Refineries Limited v. Minister of National Revenue*[1] and Judson J. in *Regal Heights v. Minister of National Revenue*[2].

For the foregoing reasons I would dismiss the present appeal with costs.

Judgment accordingly.

[1] [1949] S.C.R. 706 at 707. [2] [1960] S.C.R. 902 at 905.