Toronto 1965
Dec. 7, 8
Ottawa
Dec. 21

BETWEEN:

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

AND

CONSOLIDATED MOGUL MINES LTD.. .RESPONDENT.

Income tax—Revenue—Income Tax Act, R.S.C. 1952, c. 148, s. 83A(3)(b)—Deductions—Prospecting—Exploration and development expenses—Mining and management company—Principal business—Admissibility of evidence.

In each of the years 1957, 1958, 1959 and 1960 the appellant company sought to deduct, under the provisions of s. 83A(3) prospecting, exploration and development expenses incurred by it in searching for minerals in Canada.

The Minister disallowed the deductions on the ground that the principal business of appellant was not "mining or exploring for minerals" as required by the Section.

According to the Minister, the respondent's activities, during each of its 1957, 1958, 1959 and 1960 taxation years, were confined almost entirely to the management of its investment portfolio, to providing technical services to other companies from whom it received management fees and to arranging financing for other companies.

The evidence disclosed that respondent in each of said years had power to engage in a general mining business and exploring for minerals.

1965

MINISTER OF NATIONAL REVENUE v. CONSOLIDATED MOGUL MINES LTD.

Gibson J.

In the main during the years 1957 to 1960 inclusive, the respondent did not itself do the mining and exploring for minerals. The way it carried on business was that many claims were drawn to its attention, which claims were either held by individuals or by other companies. In most cases, neither of them had sufficient finances to explore for minerals.

The respondent in such cases entered into an arrangement of such prospects through third party limited companies. If the owner of a prospect did not have a company, a company was incorporated. If the owner of a prospect was held by another company, then this was not necessary. The respondent very often loaned money by way of debenture to such third companies and at the same time received shares from the treasury of such companies and usually entered into a contractual relationship with such companies by which it controlled the expenditure so advanced for the purpose of exploration.

Held: That the manner of conducting the mining and exploring business of the respondent is the usual and accepted one in the industry and it is permissible to use the expenditures for mining and exploring for minerals made by these third party companies as a criteria for determining whether or not the principal business of the respondent was mining or exploring for minerals within the meaning of s. 83A(3)(*b*) of the Act.

2. That mining or exploring for minerals during the years 1957 to 1960 was the respondent's principal business within the meaning of s. 83A(3)(*b*) of the Act.

3. That the appeal be dismissed with costs.

APPEAL from a decision of the Tax Appeal Board.

M. A. Mogan and *John E. Sheppard* for appellant.

John G. McDonald, Q.C. and *M. L. O'Brien* for respondent.

GIBSON J.:—This is an appeal from the Judgment of the Tax Appeal Board dated February 9, 1965 by the Minister of National Revenue in respect of the income tax assessment of the Respondent for the 1957, 1958, 1959 and 1960 taxation years.

The sole issue for determination by the Court on this appeal is whether or not the Respondent's principal business in the years 1957 to 1960 inclusive was "mining or exploring for minerals" within the meaning of s. 83A(3)(*b*) which reads as follows:

> 83A. Exploration, Prospecting and Development Expenses.
>
> (3) . . . A corporation whose principal business is
>
> . . .
>
> (*b*) mining or exploring for minerals,
>
> may deduct, in computing its income under this Part for a taxation year, the lesser of
>
> . . .

1965

MINISTER OF NATIONAL REVENUE v. CONSOLIDATED MOGUL MINES LTD.

Gibson J.

It is not disputed that the words "mining" and "exploring" in the said sub-section should be read disjunctively.

In assessing the Respondent the Appellant made the following assumptions:

(*a*) that the Respondent's income for each of its 1957, 1958, 1959 and 1960 taxation years was derived from its investments in shares, debentures and loans and from management fees received from other companies for whom it provided services of a technical nature under management contracts and that no income whatever was received from mining operations or exploring for minerals;

(*b*) that the Respondent's assets, including its available funds, were, during each of its 1957, 1958, 1959 and 1960 taxation years, almost entirely applied to its substantial invesment portfolio of shares, debentures and loans and only a very small nominal part thereof was applied to its mining assets;

(*c*) that the Respondent's activities and those of its officers and employees, were, during each of its 1957, 1958, 1959 and 1960 taxation years, confined almost entirely to the management of its substantial investment portfolio as aforesaid, the providing of management and technical services to other companies and the arranging for and the actual financing of other companies, including the underwriting of shares, the guaranteeing of loans and the lending of money to other companies and that in comparison to these activities, the Respondent's activities in the fields of mining and exploration were almost negligible; and

(*d*) that the Respondent's principal business was not, during any of its 1957, 1958, 1959 and 1960 taxation years, mining or exploring for minerals.

The assumptions in (*a*) and (*b*) above quoted are admitted by the Respondent to be correct but the Respondent disputes the assumptions in (*c*) and (*d*) above. The onus of disproving these latter assumptions is therefore on the Respondent within the meaning of *Johnston v. M.N.R.*[1]; *M.N.R. v. Pillsbury Holdings Limited*[2]; and *Talon Exploration Limited v. M.N.R.*[3]

[1] [1948] S.C.R. 186. [2] [1965] 1 Ex. C.R. 676 at 686.
[3] [1965] 1 Ex. C.R. 376 at 389 et foll

In evidence and argument the Respondent submitted that its principal business in each of the said years was mining and exploring for minerals.

The Appellant on the other hand submitted that on the evidence the principal business of the Respondent during each of the relevant years was mine management and that such submission is supported by the words used in the assumptions of the Minister which were made in assessing the Respondent and are in assumption entitled (*d*) above, namely "the providing of management and technical services to other companies".

"Mining or exploring for minerals" within the meaning of s. 83A(3)(*b*) of the Act the Respondent sought to describe and put in evidence, and it is common ground between the parties that part of Exhibit R-30, filed, probably adequately explains the details of the same as conducted in the Province of Ontario by such persons as the Respondent. Such part of said Exhibit R-30 reads as follows:

VARIOUS METHODS OF PURSUING EXPLORATION, DEVELOPMENT AND MINING ACTIVITIES

A. EXPLORATION AND MAINTENANCE OF ORGANIZATION

Presentation—Appraisal

1. Staking Claims
2. Option of Claims—(i) participant in vendor's position and purchase of shares to finance explorations—
   Formation of new company.
3. Purchase of shares in existing company.
   $0 — $25,000 Plateau—rarely $100,000.

B. DEVELOPMENT

(i) Loan of funds—least favourable.

(ii) Purchase of shares in existing company.

(iii) Direct application in wholly-owned project.
$100,000 — $500,000 plateau

C. MINING AND PRODUCTION

(i) Purchase of shares usually Control to Finance expenditures.

(ii) Creation of funded debt

(a) Simple First Mortgage

(b) Convertible to equity interest at future date.

(iii) Loan of funds to wholly-owned subsidiary or project
$500,000 — Millions required for Capital Investment.

All Instances:

(i) Isolation of Risk

(ii) Spreading and Diversification of Interests

(iii) Permits Distribution of Expenses.

1965

MINISTER OF NATIONAL REVENUE v. CONSOLIDATED MOGUL MINES LTD.

Gibson J.

"A" and "B" describe and categorize "exploring", and "C" "mining" for minerals.

From this evidence and the *viva voce* evidence adduced it was established that substantial sums of money must be expended to explore for minerals and relatively huge sums must be expended in order to mine for minerals.

The evidence also was that only a relatively few prospects for minerals after preliminary investigation are actually mined within the meaning indicated here because there must be some reasonable basis for hope of success before such sums of money will be risked by any person. It is also the evidence that of those so-called prospects which are actually explored within the meaning discussed here that only a very small number actually result in and reach the stage of mining operations within the meaning also referred to here.

Of necessity therefore the method and manner of financing, exploring and mining for minerals is difficult and specialized and takes a form or forms which are different from the financing of ordinary industrial or commercial ventures.

The evidence is that the Respondent investigated many prospects, caused the exploration of a great number, and caused or contributed to the actual mining of a few during the years 1957 to 1960. Most of the details of what was done, where and how by the Respondent are set out in Exhibit R-30.

In the main during the years 1957 to 1960 the Respondent did not itself do the mining and exploring for minerals. It caused others to do so.

In brief, the Respondent in evidence established that the way it carried on business was as follows. Many claims were drawn to its attention, which claims were either held by individuals or by other companies. Neither of them had sufficient finances to explore for minerals. If after preliminary investigation by its geologist and others the Respondent decided such prospects warranted further investigation, it entered into an arrangement with such owners of such prospects. In all cases it was done through a third party limited company. If the owner of a prospect did not have a company, a company was incorporated. If the owner of a prospect was held by another company, then this was not necessary. The Respondent very often loaned money by

way of debenture to such third party company, received shares from the treasury of such company and entered into a contractual relationship with such company by which it controlled the expenditure of the money so advanced for the purposes of exploration.

In this way, the Respondent limited its specific liability in any particular venture. It obtained a share of the equity stock in such company which would be valuable if the venture turned out to be successful. It often obtained also a fee from the third party company for what work it did or direction it gave.

On the other hand, the third party company retained part of its equity stock so that if the venture proved successful, the original owners would receive their reward.

Sometimes this process involved another strata of limited company in that the Respondent might hold shares in a third party company which in turn held shares in still another company which latter company actually did the exploring.

In one case this latter situation obtained in connection with a mining company, namely the mine in the Republic of Ireland.

This was the *modus operandi* so to speak of the Respondent during these relevant taxation years according to the evidence. The precise relationship of the Respondent to each of these third party companies with whom it was associated or connected in this fashion and what was actually advanced to such companies by the Respondent and what was received by the Respondent was not given in evidence.

The source and application of capital funds of the Respondent in connection with the Respondent's relationship with these companies was also not given in evidence.

The Court at one juncture requested that such evidence be adduced but for reasons which are not now relevant for this judgment, the same was not adduced.

But on the evidence adduced the parties in fact assumed that this was the factual situation and for the purposes of this judgment I am holding that this is so.

This evidence established that in the year 1957 the Respondent proceeded in the way above referred to, and submitted that it was in the mining business by reason of

1965

MINISTER OF NATIONAL REVENUE v. CONSOLIDATED MOGUL MINES LTD.

Gibson J.

its association with Harvey Hill Mine Limited, and in the exploration business by reason of its association with Consolidated Halliwell Limited, North Rankin Nickel Mines Limited, Coldstream Copper Mines Limited, Canam Copper Company and Irish Copper Mines Limited and others.

This evidence also established that the Respondent during the years 1958 to 1960 inclusive was in both the mining and exploration business but mainly the exploration business by reason of its association with the said companies and others, except Harvey Hill Mine Limited which had been put on a stand-by basis in 1957.

Exhibit A-1, filed by the Appellant is an analysis of the revenues and expenditures of the Respondent during the years 1956 to 1961 as taken from the records and published financial reports of the Respondent save and except the one line which is inserted under the paragraph entitled "Amounts Expended in Years 1957-1960 for Administrative Expenses and Exploration Expenses" which is described as:

Exploration expenditures incurred as agent for others

1956	1957	1958	1959	1960
$4,654,716	$1,842,545 35	$2,341,320.04	$620,785	$833,001

This line was inserted on the request of the Respondent and is filed as an exhibit and evidence of the Respondent.

This line shows the expenditures in the main made by the associated company Consolidated Halliwell Limited which incurred these expenditures on exploring for minerals within the meaning here, and it is the submission of the Respondent that these expenditures can be used for the purpose of determining that the Respondent at the same material time was also in the business of exploring for minerals.

The Respondent for the purposes of the *Income Tax Act* itself has exploring and mining expenses which were incurred prior to 1957. Under the Act it is permissible to cumulate them and they may be used by it as a deduction from income in any subsequent year without time limit.

In brief, the Respondent says that the expenditures of Consolidated Halliwell Limited and these other companies during each of the years 1957 to 1960 inclusive which the

Respondent caused them to make in the manner set out above may be used by the Respondent not for the purpose of obtaining a deduction from its income but for the purpose of determining whether or not mining or exploring for minerals during the years 1957 to 1960 was the Respondent's principal business.

The Appellant on the other hand submits that if the Respondent does not get the deduction of exploration expenses such as those incurred by Consolidated Halliwell Limited and these others, it cannot use such expenditures as criteria to be considered in the determination of whether or not the principal business of the Respondent was mining or exploring for minerals during the years 1957 to 1960 inclusive.

In other words the Respondent submits that the exploring business of Consolidated Halliwell Limited along with the exploring businesses of the other associated companies referred to in the evidence of the Respondent, cannot be used as such criteria on the basis that it is "irrational" to use the same exploration activities to establish the principal business of the Respondent as exploring for minerals.

I am of opinion that the manner of conducting the mining and exploring business of the Respondent as adduced in the evidence is the usual and accepted one in the industry and that it is not only permissible, but, indeed the only sound criterion in this case for determining the principal business of the Respondent during these taxation years. On this evidence I conclude that during each of the taxation years 1957 to 1960 inclusive the principal business of the Respondent was mining or exploring for minerals within the meaning of s. 83A(3)(*b*).

The Respondent has satisfied the onus of proving that the assumptions of the Minister above set out in paragraphs entitled (*c*) and (*d*) are wrong.

The appeal is therefore dismissed with costs.