1964
Sept. 21, 22
Nov. 6

BETWEEN:

WEST COAST PARTS CO. LTD. ....APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Revenue—Income—Income tax—Adventure or concern in the nature of trade—Meaning of "trade" and "adventure in the nature of trade"—Usual badges of trade—Lump sum payment or premium as interest or profit from property—Fixed amount included in repayment of loan in addition to principal and interest—Loan as an investment—Bonus or discount as a profit from a trade or adventure in the nature of trade—Effect of circumstances surrounding loan transaction—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4, 6 and 139(1)(e).

This appeal is from an assessment of the appellant for its 1958 taxation year under which the sum of $56,000 received by the appellant as a bonus upon a loan was assessed as income.

The appellant, a company incorporated under the laws of the Province of British Columbia, is one of a group of seven very closely related companies, basically all the shares of six of them being owned by the seventh, Transport Finance Ltd., the shares of which were owned by members of the Ferguson family. All the companies shared a common office, a common accounting staff and a common board of directors, the members of which were members of the Ferguson family. The funds of all companies except Transport Finance Ltd. were deposited in a common bank account in the name of one of the companies, although each company kept its own book of accounts. All the companies except Transport Finance Ltd., which dealt in commercial paper and one other which was dormant, were engaged in the sale and distribution of, the repair and maintenance of, or the supply of parts for Kenworth motor trucks. At the material time, the appellant was in the process of gradually liquidating its assets, having sold its inventory of parts to a subsidiary of the manufacturer of the Kenworth trucks, which had undertaken the distribution of its own parts. One of the assets of the appellant was the amount of its funds on deposit in the common bank account.

By agreement dated February 22, 1957 the appellant agreed to lend $125,000 to a group of companies, known as the Lions Equipment group, to enable them to purchase the equipment required to fulfil a contract

for testing a gas pipeline for leaks for West Coast Transmission Ltd. The agreement provided that the loan was to be repaid by payment to the appellant of $115,000 on November 1, 1957 on account of principal, and the principal balance of $10,000 on November 1, 1958, with a premium of $56,000, together with interest at 10 per cent per annum on the monies advanced from the date of the advances to date of repayment. The loan was made and subsequently repaid in 1958 with the premium and interest as set out in the agreement.

Held: That "trade" is not the same thing as "an adventure in the nature of trade" and a single transaction may well be the latter without being the former, provided it is essentially commercial.

2. That the absence of one or all of the usual badges of trade does not negative the existence of an adventure in the nature of trade.
3. That when a person enters into a contract whereby he advances money to another person on terms that it is to be repaid at a fixed time together with an additional amount, if that additional amount is described as interest there is no problem, for interest is income from property within s. 3 of the *Income Tax Act,* but when such a contract requires repayment with such an additional amount, but does not describe it as interest, it becomes a question of fact as to whether the additional payment is or is not interest or, in any event, a profit from property in the sense of revenue derived from the money advanced, but if the additional payment is the sole consideration for the use of the money, there would appear to be a very strong probability that it is interest or a payment in lieu of interest.
4. That the lump sum payment, as provided for by the agreement under consideration, not being payment merely for the use of the money, is, in the absence of very special circumstances, a profit from an adventure in the nature of trade.
5. That a money lender who advances money in the course of an established business on terms whereby he charges interest as such plus a fixed amount determined by reference to the special risk involved would count as profits from his "trade" not only the interest but the additional amount, and it follows that when a person who is not a money lender enters into such a contract and thus embarks on an adventure in the nature of the money lender's trade and earns a similar profit, he acquires a profit from an adventure in the nature of trade.
6. That it would be unrealistic to consider a transaction such as that undertaken by the appellant an investment of a prudent investor looking to a fair and safe return by way of interest.
7. That the question whether the additional amount is a payment in respect of what is referred to as "capital risk involved" is immaterial to the question whether it is profit from a money lender's trade or from an adventure in the nature of such trade. Even if such a payment can be classified as a bonus or discount rather than interest, such classification does not negative its character as a profit from a trade or adventure, even though it might negative its character as interest on money lent. Once it is established that it is not a simple case of investment, such as a purchase of a debenture at a discount, but is an adventure in the nature of trade, such distinction becomes irrelevant.
8. That the transaction entered into by the appellant, by reason of the cumulative effect of the surrounding circumstances, was an adventure

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in the nature of trade within the meaning of s. 139(1)(*e*) of the *Income Tax Act*.

9. That the appeal is dismissed.

APPEAL under the *Income Tax Act*.

The appeal was heard by the Honourable Mr. Justice Cattanach at Victoria.

D. T. Braidwood, Q.C. for appellant.

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

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

CATTANACH J. now (November 6, 1964) delivered the following judgment:

This is an appeal from an assessment under the *Income Tax Act,* R.S.C. 1952, c. 148 of West Coast Parts Co. Ltd. for its 1958 taxation year.

The appellant is a company incorporated pursuant to the laws of the Province of British Columbia with its head office at 2015 Main Street in the City of Vancouver in that Province. It was, prior to 1955, engaged in the business of trading in parts for motor vehicles and more particularly parts for Kenworth motor trucks, which were sold through sub-dealers and to users. The annual sales averaged about $700,000, of which ninety percent were in the Province of British Columbia. The appellant maintained an inventory between $150,000 and $200,000.

In the year 1955, the manufacturer of Kenworth motor trucks undertook the distribution of its own parts through a subsidiary company known as Canadian Kenworth Limited. This Company purchased all Kenworth parts owned by the appellant, whereupon the appellant began a gradual liquidation of its remaining assets.

The appellant's banking arrangements were somewhat unusual. They were described by William John Ferguson, Jr., who was the only witness at the trial.

Mr. Ferguson is presently the president and general manager of Canadian Kenworth Ltd., but at the time material to this appeal, he was the vice-president of the appellant.

The appellant was one of seven very closely related companies, (1) Transport Finance Ltd., which as the name

implies, was a company dealing in commercial paper, (2) Ferguson Truck & Equipment Co. Ltd., the distributor of Kenworth motor trucks, (3) Ferguson Automotive Parts Ltd., which repaired and maintained the motor trucks, (4) Ferguson Trucks Ltd., the distributor of Kenworth motor trucks on Vancouver Island, (5) Midwest Kenworth Sales Ltd., the distributor for Alberta, (6) Seymour Securities, Ltd., which was dormant, and (7) the appellant which, as previously intimated, engaged in the sale of truck parts.

Basically all shares in the other six companies, were owned by Transport Finance Ltd. and the shares of Transport Finance Ltd. were owned by the members of the Ferguson family. All companies shared a common office, a common accounting staff and a common board of directors. The Board consisted of W. J. Ferguson, Jr., his father W. J. Ferguson, Sr., a brother and, in some instances, his mother and sister. All major corporate decisions of each of the seven companies were made by W. J. Ferguson, Jr., his father and brother.

The funds of all the companies, except Transport Finance, Ltd., were deposited in a bank account in the name of Ferguson Truck & Equipment Co. Ltd. although each company kept a separate book of accounts. Thus the funds of all companies were intermingled, the reason given being that there was no necessity for segregation and this constituted a simpler method of doing business. Furthermore, when a bank loan was required by any one of the six companies, it was negotiated in the name of Ferguson Truck & Equipment Co. Ltd. Clearly, the affairs of the companies were closely interwoven.

On the asset side of the appellant's balance sheets for the fiscal years ending November 1956, 1957 and 1958 under the heading "Current Assets" the following item appears, "Advance receivable—Ferguson Truck & Equipment Co. Ltd." in the respective amounts of $128,680.36, $114,805.29 and $187,170.57, which represent the appellant's funds deposited in the bank account of Ferguson Truck & Equipment Co. Ltd. No interest was paid to the appellant on these deposits.

In the latter months of 1956, a group of companies consisting of Lions Equipment Limited, C. & R. Welding

Ltd., Craig & Ralston Testing Co., Ltd., Vancouver Ditching Co., Ltd., and Craig & Ralston Construction Co., Ltd., (hereinafter referred to as "the Lions Equipment group" or "the borrowers") were engaged in negotiating a contract with Canadian Bechtel Ltd., as agents for West Coast Transmission Ltd., to test a West Coast natural gas pipeline for leaks. Such work would be carried out over a period of 150 days and required highly specialized and expensive equipment, which would be of no further use after the completion of the work. This was to be a single specialized venture which had prospects of being very profitable.

The shareholders and directors of the Lions Equipment group were J. D. Craig and W. C. Ralston. Ralston was a professional engineer possessed of skill and knowledge in the particular type of work required by the proposed contract.

The amount required to be borrowed to purchase the specialized equipment needed to undertake this work was $125,000. Craig and Ralston had tried unsuccessfully over a period of time to arrange for a loan in the required amount.

A mutual friend of J. D. Craig and W. J. Ferguson, Jr. suggested that Ferguson might have funds available whereupon Craig telephoned Ferguson explaining the proposed contract between the Lions Equipment group and West Coast Transmission Ltd., the need for money to purchase the specialized equipment to perform the contract and suggesting if a loan were forthcoming, the payment of interest at the going rate for loans of this nature plus a substantial bonus. This telephone call was not made to Ferguson in his capacity as vice-president of the appellant, but as an individual, who might be in a position to make a loan, the source of the funds to do so being unknown and immaterial to Craig.

Thereupon there followed a series of conferences between the Lions Equipment group and the Fergusons and a series of meetings of the Ferguson directors and their legal and accountancy advisors as a consequence of which it was decided to make the loan, the terms and conditions of which were embodied in an agreement dated February 22, 1957, between the Lion Equipment group, as borrowers, the appellant, as lender, and Craig and Ralston, as guarantors.

Basically this agreement provides for the loan of $125,000 by the appellant to the Lion Equipment group to be advanced in two stages, $40,000 upon execution of the agreement and $85,000 upon the execution of the contract between the borrower and West Coast Transmission Ltd., such contract to be executed no later than June 1, 1957. The loan was to be repayable, as follows, $115,000 on November 1, 1957 in reduction of principal, the balance of $10,000 on November 1, 1958, plus a premium of $56,000, together with interest at 10 percent per annum on the monies advanced from the date of such advancement to date of repayment.

The amount of $40,000 was in fact advanced to the borrowers on February 28, 1957. The agreement included a provision that, if the contract between the Lions Equipment group and West Coast Transmission Ltd. were not executed by June 1, 1957, the $40,000 advanced would be forthwith repayable to the appellant with interest at 10 percent plus a premium of 45 percent. For any significance that it may have, I observe that a premium of $56,000 on $125,000 is a premium of approximately 45 percent.

However, the contract between the borrowers and West Coast Transmission Ltd. was executed and the further amount of $85,000 of the loan was advanced to the borrowers by the appellant on April 30, 1957.

The agreement between the appellant and the borrowers and guarantors also provided for collateral security being (1) a mortgage on all equipment owned or acquired (2) the hypothecation of term life insurance on the lives of Craig and Ralston, (3) the hypothecation of all of the shares in the borrowing companies and (4) an assignment of all book accounts of the borrowers subject to a prior assignment.

However, the security, above outlined, was not sufficient to discharge the loan if it became necessary to realize upon the security. In making the loan the appellant was relying on the ability of the individuals, Craig and Ralston, to perform the contract which was to be obtained.

The repayment of $115,000 on acount of principal became due on November 1, 1957. By letter dated October 22, 1957 W. J. Ferguson, Jr., wrote the borrowers advising them of the approaching due date. Payment was not made until November 29, 1957, some 28 days beyond the due date.

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The borrowers apparently encountered difficulty in performing the conditions of their contract with West Coast Transmission Ltd. and had fallen behind in the time schedule. The borrowers were in need of additional funds and accordingly approached W. J. Ferguson, Jr. for the advance of a further amount. Mr. Ferguson and his fellow directors had become alarmed at the state of the performance of the borrowers' contract and funds were not so readily available to them as on the previous occasion. They therefore declined to make a further loan.

The borrowers' need for further funds was urgent and it became necessary for them to obtain a release of the collateral security given to the appellant in order to pledge such assets as security for a loan from other sources. Therefore, the borrowers paid off the outstanding balance of the principal of their loan to the appellant, being $10,000, plus interest to the date of payment and the stipulated bonus of $56,000 on April 22, 1958, being six months prior to the maturity date of November 1, 1958.

The payment was in the total amount of $73,872.61 made up as follows:

Repayment of loan	....	$ 10,000.00
Interest:	$40,000-245 days @ 10% ..	2,684.93
	$85,000-203 days @ 10% ..	4,727.40
	$10,000-153 days @ 10% ..	419.18
	April 3 April 18	41.10
Bonus	....	56,000.00

As previously recited, the agreement between the appellant and the borrowers dated February 22, 1957 accurately represents the ultimate terms agreed upon among the parties thereto arrived at following a series of conferences between the parties and among the directors of the Ferguson group of companies. The rate of interest payable was the subject of negotiation and a rate of 10 percent was fixed as the normal rate for a loan of this nature. The term of the loan and times and amounts of the advances and repayment were also the subject of negotiation. However, Mr. Ferguson, Jr. was adamant in his testimony that the bonus of $56,000 was proffered in the initial approach by telephone by Craig on behalf of the prospective borrowers and that such amount remained

comparatively constant throughout the negotiations antecedent to the loan being made although he conceded that it was a matter of limited discussion and negotiation.

The decision of the directors of the Ferguson companies to make the loan in the name of the appellant was predicated upon the fact that the appellant was no longer actively engaged in the business of selling truck parts, but was merely liquidating its inventory on hand and receiving outstanding accounts and primarily because there was an adequate amount on hand with the appellant to make the loan, that amount being the account receivable from Ferguson Truck & Equipment Co. Ltd.

The issue for determination is whether the sum of $56,000 received by the appellant in 1958 as a bonus upon its loan, was a profit arising from an adventure or concern in the nature of trade and is, therefore, income from a business within the meaning of ss. 3, 4 and 139(1) (*e*) of the *Income Tax Act*.

By s. 3 of the *Income Tax Act* the income of a taxpayer for a taxation year for the purposes of Part I of the Act is declared to be his income from all sources and includes income for the year, *inter alia,* from all businesses. By s. 4, income from a business is declared to be, subject to the other provisions of Part I, the profit therefrom for the year and by s. 139(1) (*e*) business is defined as including a profession, calling, trade, manufacture, or undertaking of any kind whatsoever and as including an adventure or concern in the nature of trade.

The determination of the above issue must depend on the totality of the facts and surrounding circumstances of the case because no single criterion has been laid down upon which to decide whether a transaction is an investment or an adventure in the nature of trade.

It was contended by counsel for the appellant that the sum of $56,000 received by it was a bonus compensation for risk of capital on a loan receivable and was, therefore, a capital receipt and not income subject to income tax.

It is conceded by the Minister, both in argument and in his pleadings, that to be taxable, the bonus must be a profit arising from a business, within the extended definition thereof including an adventure or concern in the nature of trade. Therefore, as stated before, the issue

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resolves itself into whether the transaction entered into by the appellant as described above, constitutes an adventure or concern in the nature of trade and not an investment.

Counsel for the appellant, after an exhaustive review of the authorities and by reference to definitions in standard dictionaries, submitted that the word "trade" has reference to a commercial or mercantile occupation of a continuing or habitual character with particular emphasis on dealing in goods or commodities. He submitted that the usual badges of trade were lacking in the transaction under review in that (1) there was no organization set up for the purpose, (2) there was no multiplicity of transactions, (3) the appellant had no prior association with the business and (4) there was no scheme, system, business or operation.

However, "trade" is not the same thing as "an adventure in the nature of trade". A single transaction may well be the latter without being the former, provided it is essentially commercial. The absence of one or all of the usual badges of trade does not negative the existence of an adventure in the nature of trade.

In *M.N.R. v. Taylor*[1] the former President of this Court points out that while the words, "adventure or concern in the nature of trade" first appeared in a Canadian *Income Tax Act* in the 1948 Act, they have been in the United Kingdom *Income Tax Acts* since 1842. He then proceeds to a careful examination of the leading cases dealing with the meaning of the expression and arrives inductively at certain general propositions to guide the Court in dealing with a particular case. He first advances some negative propositions concerned with excluding a number of erroneous tests.

On the negative side he had this to say:

(i) The singleness or isolation of a transaction cannot be a test of whether it was an adventure in the nature of trade . . . it is the nature of the transaction, not its singleness or isolation that is to be determined.

(ii) It is not "essential to a transaction being an adventure in the nature of trade that an organization be set up to carry it into effect".

(iii) ". . . the fact that a transaction is totally different in nature from any of the other activities of the taxpayer and that he has never entered upon a transaction of that kind before or since does not, of itself, take it out of the category of being an adventure in the nature of trade."

[1] [1956] C.T.C. 189; 56 D.T.C. 1125.

(iv) "The intention to sell the purchased property at a profit is not of itself a test of whether the profit is subject to tax for the intention to make a profit may be just as much the purpose of an investment transaction as of a trading one. The considerations prompting the transaction may be of such a business nature as to invest it with the character of an adventure in the nature of trade even without any intention of making a profit on the sale of the purchased commodity."

On the positive side the former President outlines some specific guides:

(i) ". . . if a person deals with the commodity purchased by him in the same way as a dealer in it would ordinarily do such a dealing is a trading adventure."

(ii) The nature and quantity of the subject matter of the transaction "may exclude the possibility that its sale was the realization of an investment or otherwise of a capital nature or that it could have been disposed of otherwise than as a trade transaction."

While formulating these guides as helpful, he recognizes that the question whether a particular transaction is an adventure in the nature of trade depends on its character and surrounding circumstances and no single criterion can be formulated.

When a person enters into a contract whereby he advances money to another person on terms that it is to be repaid at a fixed time together with an additional amount, if that additional amount is described as interest, there is no problem. Interest is income from property within s. 3 of the *Income Tax Act* and it is specifically required to be included in computing income by s. 6. When such a contract requires repayment with such an additional amount, but does not describe it as interest, it becomes a question of fact as to whether the additional payment is or is not in fact interest or, in any event, a profit from property in the sense of revenue derived from the money advanced. If the additional payment is the sole consideration for use of the money, there would appear to be a very strong probability that it is interest or payment in lieu of interest. The problem is more complicated where, as here, the contract provides for repayment with interest as such plus an additional fixed amount. Usually the promise of such an amount is not regarded as being a payment for the use of the money, but as an inducement to the lender to incur the risk of not getting his money back in speculative circumstances. I cannot escape the conclusion that, in such event, the lump sum payment, not being payment

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merely for the use of the money, is, in the absence of very special circumstances, a profit from an adventure in the nature of trade.

There can be no doubt that a money lender who advances money in the course of an established business on terms whereby he charges interest as such plus a fixed amount determined by reference to the special risk involved, would count as profits from his "trade" not only the interest collected as such, but the additional amounts charged by reason of special risks. If it be true that such an amount is a profit from a money lender's trade, it follows, in my view, that, when a person who is not a money lender enters into such a contract and thus embarks on an adventure in the nature of the money lender's trade and earns a similar profit, he acquired a profit from an adventure in the nature of trade.

In the present instance the borrowers did not approach the appellant to obtain the loan, but rather Mr. W. J. Ferguson, Jr. in his personal capacity, who in turn discussed the proposition with his fellow directors who, as I have indicated, were directors of all seven companies in the Ferguson group. The decision to grant the loan was not entered into lightly. The advantages and disadvantages were carefully weighed and the lenders obtained as much collateral security as possible, but the security so obtained was not sufficient to cover the loan in event of default. The prime factor which influenced the grant of the loan was the reliance placed on the prospect of the borrowers making a substantial profit from the pipeline testing contract, which was virtually assured. After a very careful appraisal of the risks involved the directors of the Ferguson group decided to make the loan.

The word "adventure" is defined in the Shorter Oxford Dictionary as a "pecuniary venture" and "a speculation". The word, "venture" is in turn defined as meaning "a commercial enterprise in which there is a considerable risk of loss as well as a chance of gain". There is no doubt that the risk of loss was a paramount consideration present in the minds of the directors of the Ferguson companies and it is equally clear that the chance of substantial gain, namely, a bonus of $56,000 or in terms of percentage 45 percent on the principal sum, offset the risk of loss and was the determining factor in the decision to make the loan. To me

it would be unrealistic to consider a transaction such as this as an investment of a prudent investor looking to a fair and safe return by way of interest. There is no doubt that the prospect of a very substantial premium within a very short period of time was the dominant consideration.

The directors of the appellant were not unfamiliar with the finance and loan business. Transport Finance Ltd., of which they were also directors, was engaged in the business of financing motor vehicles sold by the other related companies and a loan with a substantial bonus was made by Ferguson Automotive Parts Ltd. to oblige a customer of the Ferguson interests, prior to the present loan.

In my view, what the appellant did here is precisely what an ordinary money lender would do.

I should also say that, in my view, the question whether the additional amount is a payment in respect of what is referred to as "capital risk involved" is immaterial to the question whether it is profit from a money lender's trade or from an adventure in the natue of such trade. Even if such a payment can be classified as a bonus or discount rather than interest (cf *Lomax v. Peter Dixon & Son Ltd.*)[1], such classification does not negative its character as a profit from the trade or adventure, even though it might negative its character as interest on money loaned. Once it is established that this is not a simple case of investment, such as the purchase of a debenture at a discount, but is an adventure in the nature of trade, such distinction becomes irrelevant.

I am, therefore, of the opinion that this transaction entered into by the appellant, by reason of the cumulative effect of the surrounding circumstances, was an adventure in the nature of trade within the meaning of s. 139(1)(*e*) of the *Income Tax Act,* that the profit from it was a profit from a business within the meaning of s. 3 of the Act and that the Minister was, therefore, right in including the premium of $56,000 in the appellant's assessment for its 1958 taxation year.

The appeal is, therefore, dismissed with costs.

Judgment accordingly.

[1] 25 T.C. 353.