1944
Sep. 7.
1946
Jun. 25.

BETWEEN:

THE ECONOMIC TRUST COMPANY .. APPELLANT,

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

Revenue—Income Tax—Income War Tax Act, R.S.C. 1927, c. 97, s-6 (b)—Distinction between capital loss and loss in an operation of business or in carrying out a scheme of profit making—Distinction between fixed and circulating capital—Loss on sale of shares in course of business deductible.

Appellant was incorporated by a private act and had power to purchase and resell mortgages, debentures, bonds and capital stocks. It did not operate as a trust company in that it did not administer estates or act as executor, but it managed investments for its clients. It also bought and sold securities on its own account with a view to making a profit thereon. In 1941 it sold certain shares and sustained a loss thereon which it sought to deduct as a loss incurred in the course of its business. The claim for deduction was disallowed on the ground that it was a capital loss within the meaning of section 6 (*b*) of the Act.

Held: That the loss made by the appellant in 1941 was incurred in the ordinary course of its business as dealer in securities, that it must be considered as a loss of profit and not as capital loss, and that the appellant was justified in deducting this loss from its profits for the year 1941.

APPEAL under the provisions of the Income War Tax Act.

The appeal was heard before the Honourable Mr. Justice Angers, at Winnipeg.

H. G. Harvey Smith for appellant.

Ward Hollands, K.C. and *A. A. McGrory* for respondent.

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

Angers J. now (June 25, 1946) delivered the following judgment:

This is an appeal under sections 58 and following of the Income War Tax Act, 1917, and amendments thereto, from the assessment of the appellant, dated September 19, 1942, whereby a tax in the sum of $312.11 was levied in respect of income tax for the year 1941.

The appellant was incorporated by a private act of the legislature of the Province of Manitoba intituled An act to incorporate "The Economic Trust Company" assented to on February 26, 1908, being chapter 76 of 7-8 Edward VII.

In its return of income and excess profits tax for the fiscal year ended December 31, 1941, bearing date April 30, 1942, the appellant showed that there was no income taxable.

A notice of assessment was mailed by the Commissioner of Income Tax to the appellant on September 19, 1942, showing a taxable income of $1,733.93 an income tax at 18% thereon amounting to $312.11 and interest of $6.90 to October 19, 1942, date of payment.

A notice of appeal dated October 16, 1942, was sent to The Minister of National Revenue by appellant's solicitors. This notice, after stating that by its act of incorporation very wide powers were given to the appellant company, refers particularly to section 13 of which the following may be quoted:

It shall be lawful for the company to acquire, by purchase or otherwise, mortgages upon real estate and debentures of municipal or other corporations, or school districts, and bonds, debentures or capital stock of any incorporated company, and to resell the same, and to invest any moneys forming part of their capital or reserve, or accumulated profits,

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in such securities, real and personal, and to mortgage sell or otherwise dispose of the same, or any part thereof. and to re-invest the proceeds, as the directors may from time to time deem expedient.

The notice of appeal then relates that prior to the taxation year 1941 the Company had acquired 100 shares without par value of Canadian Northern Power Corporation Limited, 37 shares without par value of Carnegie Finance and Investment Company Limited and 75 shares without par value of Imperial Oil Limited, all of which were sold during the year 1941, resulting in a loss of $2,607.92. The notice goes on to say that the Company regards and has treated this amount of $2,607.92 as a loss incurred in its operations and accordingly has carried it into its balance sheets as a loss, reducing its net profit for the year 1941 to $557.39. The notice then states that the sum of $1,431.38 comprises dividends on stocks of Canadian companies and is not subject to payment of income tax in the hands of the appellant and that the latter therefore had no income subject to taxation in the year 1941.

The notice of appeal concludes thus:

The Assessment appealed from proceeds on the assumption that the item of $2,607.92 is not deductible from income.

The Economic Trust Company appeals from the foregoing assessment on the ground that the loss, in the sum of $2,607.92 was incurred by the Company as an operating loss of the business of the Company under the powers and authorities contained in and conferred by its Act of Incorporation.

That such loss is not a capital loss, but a loss in operations resulting from the normal business of the Company in exercise of the powers given to it under section 13 quoted above.

That for the Taxatoin year 1936 the Company's income tax return showed a profit made on the sale of bonds, which profit was included in its taxable income, and for which profit the Company was assessed and paid income tax.

That for the Taxation year 1936 the Company's income tax return showed a profit on the sale of bonds and a loss on the sale of real estate, both of which were accepted as proper by the taxing authority and were allowed, and the Company was not assessed for income tax for that year.

The decision of the Minister of National Revenue, dated February 3rd, 1944, affirming the assessment, contains (inter alia) the following statements:

The Honourable the Minister of National Revenue having duly considered the facts as set forth in the Notice of Appeal and matters thereto relating hereby affirms the said Assessment on the ground that the loss claimed by the taxpayer as a deduction from its income was properly disallowed for Income Tax purposes under and by reason of the

provisions of Section 6 (b) of the Act and on these and related grounds and other provisions of the Income War Tax Act in that respect made and provided the Assessment is affirmed.

Notice of such decision is hereby given pursuant to Section 59 of the Act and is based on the facts presently before the Minister.

The appellant dissatisfied with the decision of the Minister, in accordance with section 60 of the Act mailed to the latter a notice of dissatisfaction in which it recapitulated the facts, statutory provisions and reasons which it intends to submit to the Court in support of its appeal.

After referring to the act of incorporation of the appellant company and quoting a part of section 13 thereof dealing with the investment of the Company's funds, the appellant repeated the main statements of its notice of appeal adding thereto the following, which seems to me material:

The purchase and resale of securities constitute part of the business of the Appellant and are authorized by its Act of Incorporation and such transactions are engaged in by the Appellant for the purpose of making profits and are acts done in the carrying on or carrying out of its business.

(*b*) The Economic Trust Company appeals from the foregoing assessment on the ground that the loss, in the sum of $2,607.92 was incurred by the Company as an operating loss of the business of the Company under the powers and authorities contained in and conferred by its Act of Incorporation.

The capital employed by the Appellant in connection with the purchase and resale of the securities in question was not fixed but circulating capital of the Appellant used by it in the normal and ordinary carrying on or carrying out of its business as authorized by Section 13 of its Act of Incorporation.

The Appellant will submit that Section 6 (b) of The Income War Tax Act has no application to the losses in question as the said section applies only to losses of fixed capital and that losses sustained in the ordinary carrying on of the Appellant's business are not affected by the said section.

The Minister in his reply denies the allegations of the notice of appeal and the notice of dissatisfaction in so far as incompatible with the allegations of his decision and affirms the assessment as levied.

Counsel for appellant in opening said that the loss of $2,607.92 for the taxation year 1941, shown in the profit and loss account attached to the appellant's return, arose through the sale of securities referred to in the notice of dissatisfaction and that this loss was deducted from the profits of the Company, which, naturally, were reduced accordingly.

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Counsel pointed out that the profit and loss account shows a difference of $3,165.31 between revenue and expenditure and that, when the amount of the loss aforesaid is deducted from this difference, the net profit for this year is reduced to $557.39. He drew the attention of the Court to the fact that against that there are dividends payable to appellant by Canadian companies totalling $1,431.38, altogether exempt from taxation. So, in his view, we have the situation that, after having accepted as a deduction from the profit the loss of $2,607.92 the net profit left to appellant for the year 1941 is $557.39.

Evidence was adduced, a brief resume whereof seems apposite.

Elmer Woods, general manager of Oldfield, Kirby and Gardner Limited, of the City of Winnipeg, and director of the appellant company, testified that Oldfield, Kirby and Gardner Limited manage the appellant company.

Asked to describe the nature of the appellant company Woods made the following statement (p. 6):

> Well, it manages mortgage investments of private clients; it buys mortgages on its own account, stocks or bonds, or other types of securities as permitted to do by the charter. It does not administer estates or act as executor or administrator of estates.

He added that in that respect it is unlike an ordinary trust company.

He declared that the clients' funds are dealt with separately as trustee for the clients and that the company's own funds are kept separate.

He said that the company makes its profits by way of fees in the management of clients' mortgages, interest and dividends from stocks and bonds and gains made on the purchase or sale of the latter.

Dealing with the policy followed by the company in the use of its own funds, Woods set forth the following remarks (p. 8):

> When the Company has funds available we are governed in the use of those funds and the use we will put them to by the condition of the market at that particular time. At certain periods mortgages either were not available, in which case we would seek to purchase stocks or bonds, from which we could get capital appreciation or income as well, or there were periods when we did not think the security market was such that it was attractive to make investments in, and then we would seek out a mortgage market. At times we would have funds available we would not use for mortgages or stocks and bonds, but depending on

the condition existing at the particular time the funds were available, it would depend on how we would use them, and that has gone on—well, prior to my connection with the Company, perhaps twenty years or more.

Later he observed that in the past few years the company has had by far the largest part of its capital invested in stocks and bonds and a small part in mortgages owing to the adverse effect of debt legislation on mortgages in Manitoba.

Asked in what way the debt adjustment legislation would affect his judgment in dealing with mortgages Woods replied (p. 8[a]):

> Well, with farm mortgages, under the Farmers Creditors Arrangement Act the Court had the right to reduce the amount owing on the mortgage, in which case you might buy a mortgage and you would think you had security for a certain amount of money, only to find within reasonable time or some time after that the mortgage principal was cut in half; and in the city, on residential property, by debt adjustment legislation, the Debt Adjustment Board had a right to postpone payments over a long period of time, and while they did not have the right to reduce the principal, they had the right to change the terms of a mortgage, which would seriously upset your investment program. In other words, the right of foreclosure was taken away on city property.

He added that mortgages lost their "marketability" feature and that no one wanted them. According to him the mortgagee companies and trust companies have largely switched the use of their capital from mortgages to stocks and bonds.

He declared that the appellant proposed to make money in dealing with various types of securities, through the increase in the market value of the securities it bought and the disposal thereof at a profit.

Woods was asked to tell the reason why the appellant in 1941 sold shares of Canadian Northern Power Corporation, shares of Carnegie Finance and Investment Company Limited and shares of Imperial Oil Limited, all acquired before the taxation year 1941; he gave the following information (p. 11):

> I don't think I can answer that question specifically because I don't remember those three particular transactions, but the reason in all cases why securities are sold is because at that particular time we usually have some other security we want to reinvest in that we think has a better opportunity for market appreciation. We may have felt these securities had either reached a price that was as much as they were worth, and something else we had reinvested in had not, or we might have felt at

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that time that the prospects for these particular Companies were not bright enough to warrant our continuing to hold the security. But I can't tell you what prompted us in making these sales in that way.

He added that those were the general principles which govern his company in the sale of securities.

In cross-examination Woods said that the appellant does not carry on the business of a trust company but that it has the powers to do so.

He stated that the company acts for clients who entrust their money to it, that it charges them a fee for looking after their affairs and that it derives a profit in carrying on that business.

John D. Reid, chartered accountant, of the firm of John D. Reid & Company, of Winnipeg, auditors for the appellant company since 1936, testified that he is familiar with its books and has examined them. Shown the notice of assessment for the year 1941 mailed to The Economic Trust Company on September 19, 1942 above-mentioned, he said that he studied it and that he prepared the appellant's income tax return for 1941.

It appears from this return, as it did from the company's records according to the witness, that the net income for the fiscal year 1941 was $557.39 and that the dividends received from Canadian companies amounted to $1,431.38.

He stated that he prepared the auditors' report and the profit and loss account filed with the company's income tax return and that he is familiar with these documents.

The profit and loss account shows the revenue of the company for the year 1941 as being $5,650.49 and the expenditure $2,485.18, thus leaving a balance of $3,165.31. The said account further shows a net loss on stocks and bonds sold amounting to $2,607.92, which deducted from the balance of $3,165.31 leaves a net profit of $557.39.

On counsel's request Reid enumerated the items of the revenue, as they appear in the profit and loss account. This enumeration, in my view, was superfluous.

Coming to the item of $2,607.92 for the loss on stocks and bonds sold, Reid shared it as follows: on Dominion of Canada bonds acquired in 1940 a loss of $12.50; on Imperial Oil shares bought in 1937 a loss of $946.50; on shares of Canadian Northern Power Corporation Limited purchased in 1936 a loss of $1,800.25. These losses totalled $2,759.25,

as the witness rightly pointed out. Reid declared that the shares in Carnegie Finance & Investment Company Limited were sold with a profit of $151.33. Subtracting this sum of $151.33 from that of $2,759.25 there remains a net loss of $2,607.92, mentioned as the item deducted in the profit and loss account.

Reid declared that to arrive at the figure of $1,733.93 for the taxable income the Department of National Revenue added to the sum of $557.39 mentioned in the company's return as being the net profit for the year 1941 the amount of the loss on stocks and bonds sold in the sum of $2,607.92 as indicated in the profit and loss account, which makes a total of $3,165.31. Reid said that this is the figure which the Department considered as being the company's net profit up to that point. He stated however that the Department allows a deduction for the dividends from Canadian corporations which totalled $1,431.38, thus reducing the net profit to $1,793.33 shown as being the taxable income in the notice of assessment.

He declared that he studied the books of the company and that he is familiar with the various business transactions therein disclosed. The witness was requested to tell the Court the nature of purchases and sales of securities. On the suggestion of counsel for plaintiff, Reid produced a statement prepared by himself showing the purchases and sales of stocks and bonds in the years 1927 to 1943, with the exception of the years 1930 to 1934. This statement, filed as exhibit 1, is self-explanatory and I do not think that an analysis of it herein would serve any useful purpose, apart from the fact that it would enlarge these already copious notes.

Counsel for appellant produced as exhibit 2 a summary statement of assets of the company for the years 1926 to 1943 inclusive.

This second statement shows a change in the nature of the assets of the company from 1926. For instance the amount of the mortgages in 1926 was $98,809. It decreased gradually until in 1941 it reached a minimum of $11,287. On the other hand in 1926 the common stocks amounted to $50,560 while in 1927 they had fallen down to $1,310 and in 1928 to $765. The statement exhibit 2 shows that in the

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years 1929 to 1935 inclusive the company held no common stocks. In 1936 it had $5,160 worth of them and in the following years the amount increased gradually from $16,499 in 1937 to $54,843 in 1941. It discloses that the bonds totalled $25,825 in 1927, $35,450 in 1928, decreased to $9,625 in 1929 and stayed at that figure until 1934, amounted to $16,635 in 1935, $13,327 in 1936, $10,557 in 1937, 1938 and 1939, disappeared totally in 1940 and amounted to $35,407 in 1941. In brief there were in 1941 as assets: $11,287 in mortgages, $10,300 in preferred stocks, $54,843 in common stocks and $35,407 in bonds.

Reid stated that the uses to which the company was putting these funds changed according to its policy and conditions and that it is the same money changing from mortgages to stocks and bonds. He asserted that the money shown in these figures had nothing to do with clients' funds.

He declared that the clients' funds are handled entirely in a trust account, deposited in a separate bank account and entered in separate ledgers.

Asked if the securities sold in 1941 had anything to do with clients' trust funds, Reid replied that they had not, adding that they were the company's own funds.

In cross-examination Reid declared that, as appears in the balance sheet annexed to the return, the clients' funds in 1941 amounted to $310,437.79.

Counsel for respondent said he had no evidence to adduce.

The point at issue is whether the sum of $2,607.92 charged against the revenue as being a loss on stocks and bonds was a capital loss or whether it was a loss incurred in the ordinary course of business. The reason which makes it necessary to elucidate this question is the reliance placed by the respondent on subsection (*b*) of section 6 of the Income War Tax Act, which says:

> In computing the amount of the profits or gains to be assessed, a deduction shall not be allowed in respect of
> (*b*) any outlay, loss or replacement of capital or any payment on account of capital or any depreciation, depletion or obsolescence, except as otherwise provided in this Act.

It was submitted by counsel for appellant that practically all the cases reported deal with the taxability of profits and that these cases have mostly been decided on the basis of

the Department of National Revenue seeking to tax profits originating by way of capital appreciation of securities or other assets. Counsel pointed out that this is the general trend of the numerous cases but that the present case is the converse, since it deals with the right of the tax-payer to deduct from his income losses incurred in the sale of securities. It was argued by counsel for appellant that the same principles will apply in determining whether these losses are capital losses or losses incurred in the course of business. Counsel particularly drew the attention of the Court to the fact that, when he refers to these cases the same principles apply for deduction of losses as apply in the taxability of profits.

It was urged on behalf of appellant that it is the first part of section 13 of the Act incorporating The Economic Trust Company which gives the company the power to acquire, by purchase or otherwise, mortgages, bonds, debentures or capital stock of any incorporated company and to sell or otherwise dispose of them and that there is no restriction contained in the Act in that regard, although it is possible that the company is restricted to certain types of securities in accordance with the sections concerning trust companies in the Manitoba Companies Act.

Counsel insisted that the appellant company is by its charter given just as wide powers to acquire and sell securities as an ordinary trading company would have to buy and sell merchandise. He pleaded that these powers were exercised by the company as part of its business with the object of making a profit for itself. In counsel's view that is the main difference between an ordinary trust company's activities and those of the appellant company. He observed that an ordinary trust company manages its clients' affairs and that it derives its income from transfer fees and management fees, particularly the management of estates with which the appellant has nothing to do.

Counsel submitted that the test for deciding whether or not appreciation or losses in the sale of securities become taxable income is a simple one and has been laid down in a great number of cases. He summed up the test sub-

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stantially thus: did the losses result from acts done in the carrying on of a business or in an operation of business in carrying out a scheme for profit making?

Counsel relied on various authorities upon which, I believe, it will suffice to comment briefly. I shall refer to them in their order of citation.

Konstam, The Law of Income Tax, 9th ed., where at page 104 the author says:

> Controversy often arises as to whether the net proceeds of sales of investments in securities, landed property and so on are profits of a trade or accretions of capital. The test is, whether or not a trade is carried on in the buying and selling of the investments. Thus, a man who possesses a collection of pictures for his own enjoyment, and who sells one of them to meet his pecuniary necessities—or even because a tempting offer happens to be made to him—is not taxable for the proceeds of the sale; but a picture dealer who has bought to sell again is liable on his net profits.

The author then quotes an extract from the judgment in the case of *Californian Copper Syndicate* v. *Harris* (1); and also an extract from the judgment in the case of *Jones* v. *Leeming* (2). Konstam thereafter adds:

> In practice the line is often difficult to draw. The buying and selling of investments is a necessity of insurance business; and where an insurance company in the course of its trade realises an investment at a larger price than was paid for it, the difference is to be reckoned among its profits; conversely, any loss is to be deducted. An investment company (so named) which had power to vary its investments was taxable on the profits made by realising securities, though these were not distributed as dividend but were credited to capital account, and although the capital account as a whole showed a loss in the year in question; and a bank was taxable on the profits shown as a result of the conversion of National War Bonds held by it.

Counsel for appellant then referred to the case of *Californian Copper Syndicate* v. *Harris (ubi supra)*, mentioned by Konstam, in which Clerk, L.J. expressed the following opinion (p. 165):

> 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 realise 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 realisation or conversion of securities may be so assessable, where what is done is not merely a realisation or change of investment, but an act done in what is truly the carrying on, or carrying out, of a business. The simplest case is that of a person or association of persons buying and selling lands

(1) (1904) 5 T.C. 159, 165. (2) (1930) A.C. 415, 420.

or securities speculatively, in order to make gain, dealing in such investments as a business, and thereby seeking to make profits. There are many companies which in their very inception are formed for such a purpose, and in these cases it is not doubtful that, where they make a gain by a realisation, the gain they make is liable to be assessed for Income Tax.

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 realising a security, or is it a gain made in an operation of business in carrying out a scheme for profit-making?

Lord Trayner made these observations (p. 167):

I agree with your Lordships that the determination of the Commissioners is right. This is not, in my opinion, the case of a company selling part of its property for a higher price than it had paid for it, and keeping that price as part of its capital, nor a case of a company merely changing the investment of its capital to pecuniary advantage. My reading of the Appellant Company's Articles of Association along with the other statements in the case satisfy me that the sale on which the advantage was gained, in respect of which Income Tax is said to be payable, was a proper trading transaction, one within the Company's power under their Articles, and contemplated as well as authorised by their Articles. I am satisfied that the Appellant Company was formed in order to acquire certain mineral fields or workings—not to work the same themselves for the benefit of the Company, but solely with the view and purpose of reselling the same at a profit. The facts before us all point to this.

Counsel then relied on the remarks of Lord Dunedin in the case of *Commissioner of Taxes* v. *Melbourne Trust Limited* (1), where at page 1010 is quoted a part of the reasons set forth in *Californian Copper Syndicate* v. *Harris* hereinabove reproduced. Following the quotation Lord Dunedin added:

In the present case the whole object of the company was to hold and nurse the securities it held, and to sell them at a profit when convenient occasion presented itself.

At this point counsel pointed out that Elmer Wood declared that the reason why the appellant company bought the securities with which we are concerned and sold them later was for the purpose of making profits and that it would not have been able to carry out this scheme if it had not been for its wide powers under section 13 of the Act of Incorporation.

(1) (1914) A.C. 1001.

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Counsel then referred to the decision of the House of Lords in re *Ducker* v. *Rees Roturbo Development Syndicate, Limited* and *Commissioners of Inland Revenue* v. *Rees Roturbo Development Syndicate, Limited* (1) particularly to the opinion expressed by Lord Buckmaster at page 140:

> My Lords, I think it is undesirable in these cases to attempt to repeat in different words a rule or principle which has already been found applicable and has received judicial approval, and I find that in the case of the *Californian Copper Syndicate* v. *Harris* it is declared that in considering a matter similar to the present the test to be applied is whether the amount in dispute was "a gain made in an operation of business in carrying out a scheme for profit-making." That principle was approved in a judgment of the Privy Council in the case of *Commissioner of Taxes* v. *Melbourne Trust,* and it is, I think, the right principle to apply.

Counsel for appellant then referred to Plaxton, Canadian Income Tax Law, 1939 ed., p. 144, where the author states:

> A profit or gain derived from the realization of a capital asset with a view to substituting some other form of investment should be distinguished, therefore, from a profit or gain realized in the course of carrying on a trade or business. If the profit or gain is merely the result of realizing the enhancement of value of an asset, it is a capital accretion and not subject to tax while if it is a profit or gain made in an operation of business in carrying out a scheme for profit making it is income and subject to tax. The line which separates the two classes is difficult to define and each case must be considered according to its facts, the decisive question being whether or not a trade or business is carried on.

There are many cases cited by Plaxton besides those already referred to, which add very little if anything to the subject under examination.

At page 139 of his book Plaxton makes these comments, which are indeed pertinent:

> Operations contemplated and authorized by the Memorandum of Association or Charter of a Company have been held to be operations in the carrying on of the Company's business, even though speculative and isolated transactions. But the mere fact that the power to sell any part of the undertaking and property of the Company is included in the Company's Memorandum of Association, when taken in conjunction with the ultimate sale of the entire assets of the Company to a new company is not conclusive that the company is carrying on the trade of purchasing and selling land.

The author, at page 144, refers to the case of *Californian Copper Syndicate* v. *Harris (ubi supra)*; a passage from the judgment therein is hereinabove quoted. The company,

(1) (1928) A.C. 132.

as appears from the report, had been formed for the object of acquiring and reselling mining properties at a profit. Where the company acquired and sold such properties, even though it was a single transaction, it was held to be taxable.

Reference may also be had to the following cases, which have some relevance to the problem at issue: *T. Beynon and Company, Limited v. Ogg* (1); *Gloucester Railway Carriage* and *Wagon Company, Limited* v. *Commissioners of Inland Revenue* (2).

The facts in the case of *T. Beynon and Company, Limited* v. *Ogg* are set forth in the headnote, which is a fair and adequate summary of the decision; it reads thus:

A Company carrying on business as Coal Merchants, Ship and Insurance Brokers, and as sole selling agent for various Colliery Companies, in which latter capacity it is part of its duty to purchase wagons on behalf of its clients, makes a purchase of wagons on its own account as a speculation and subsequently disposes of them at a profit. It was contended that, this transaction being 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 the liability of the Company to Income Tax.

Held, that the profit realised on this transaction was made in the operation of the Company's business and was properly included in the computation of the Company's profits for assessment under Schedule D.

At page 133 of the report we find this interesting statement by Mr. Justice Sankey:

My attention was called by the Attorney-General to the case of *Californian Copper Syndicate* v. *Harris* 5 Tax Cases, page 159. Having regard to the remarks which were made on that case in the two subsequent cases to which I have been referred, particularly in the case of *Tebrau (Johore) Rubber Syndicate* v. *Farmer* (5 T.C. 658) I am not sure whether the *Californian Copper Syndicate* v. *Harris* is a case which one ought to follow unless one had facts which were nearly identical with the facts in that particular decision. But I think the present position really goes beyond the Californian case. I think that there was evidence here that this transaction was a transaction, and this profit was a profit, made in the operation of the Appellant Company's business. I do not for a moment intend to endeavour to define where the line ought to be drawn. I do not think it is desirable, and I am perfectly satisfied that I am not capable of doing it, but it is perfectly easy to say whether Case A or Case B falls on the one side or the other; and for the reasons which I have endeavoured to give I think that the Commissioners were right in their determination as to which side of the line this case fell, and in the result I must uphold their determination.

(1) (1918) 7 Tax Cases, 125. (2) (1925) A.C. 469.

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In the case of *Gloucester Railway Carriage and Wagon Company, Limited* v. *Commissioners of Inland Revenue* the headnote contains a substantial and comprehensive summary of the facts and decision; it is worded as follows:

A company manufactured railway wagons and dealt with them either by selling them (outright or under hire purchase agreements) or by letting them on hire. In the books of the company the wagons owned by the company and let on hire were capitalized at a sum which included a calculated sum added as profit on manufacture and a certain amount was written off the value year by year for depreciation. The company having decided to sell all the wagons used for letting on hire, sold them at sums larger than the sums at which the wagons then stood in the books. In assessing the company to corporation profits tax the surplus obtained from the sale of these wagons was included as a trade profit of the company, and on appeal the Special Commissioners, in affirming the assessment, found that the business of the company was a single business—namely, to make a profit in one way or another out of manufacturing wagons:—

Held, that the surplus in question was not a capital accretion, but was rightly included as a trade profit for the purposes of the corporation profits tax.

Another case referred to is that of *Anderson Logging Company and The King.* The judgment of the Supreme Court of Canada reported in (1925) S.C.R., 45, was subsequently affirmed by the Privy Council, whose decision is found in (1926) A.C., 140.

The headnote in the Supreme Court reports, fair and sufficiently comprehensive, is in the following terms:

Where the powers of a company, incorporated to take over as a going concern a logging business, included the power to acquire timber lands with a view to dealing in them and turning them to account for the profit of the company, and it bought a tract of timber land and sold it at a profit the same is not a capital profit but one derived from the business of the company and as such assessable to income tax under section 36 of the Income and Personal Property Taxation Act (B.C.) 1921, 2nd Sess., (p. 48):

A quotation from the notes of Mr. Justice Duff, as he then was, later Chief Justice of Canada, seems apposite (p. 48):

The principle of these decisions can best be stated for our present purpose in the language of Lord Dunedin in his judgment delivered on behalf of the Judicial Committee, in *Commissioner of Taxes* v. *The Melbourne Trust, Ltd.* (1914, A.C. 1001, at pp. 1009 and 1010).

It is common ground that a company, if a trading company and making profit, is assessable to income tax for that profit . . . . The principle is correctly stated in the Scottish case quoted, *California Copper Syndicate* v. *Harris* (6 F., 894; 5 T.C. 159). It is quite a well settled principle in dealing with questions 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 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;

or, in the language of the judgment from which this quotation is made, which follows in sequence after the passage cited:

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?

or, in the form adopted by Sankey J.—in *Beynon* v. *Ogg* (1918, 7 T.C. 125, at p. 132)—from the argument of the Attorney General—was the profit in question a profit made in the operatoin of the appellant company's business?

Mr. Justice Duff then adds:

The appellant company is a company incorporated for the purpose of making a profit by carrying on business in various ways including, as already mentioned, by buying timber lands and dealing in them. It is difficult to discover any reason derived from the history of the operations of the company for thinking that in buying these timber limits the company did not envisage the course it actually pursued for turning these limits to account for its profit as at least a possible contingency; and, assuming that the correct inference from the true facts is that the limits were purchased with the intention of turning them to account for profit in any way which might present itself as the most convenient, including the sale of them, the proper conclusion seems to be that the assessor was right in treating this profit as income.

Counsel for appellant further contended that the securities on the sale whereof the loss was incurred constituted circulating capital and not fixed capital and that as such the profits realized thereon were subject to income tax and the loss resulting from their sale was accordingly deductible. Reference was made to Plaxton's work, where at page 147 are the following observations:

A further means of differentiating the two classes is afforded by the distinction drawn by economists between fixed capital (property acquired and intended for retention and employment for the purposes of production) and circulating capital (property acquired or produced with a view to resale or a sale at a profit). As a general rule, the realization of the enhanced value of fixed capital is not assessable as income, whereas a profit or gain made in the turning over of circulating capital is a profit or gain made from carrying on business, and as such is assessable to income tax.

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Counsel observed that, if the loss is sustained in circulating capital it may be deducted as a loss for income tax purposes, as not being capital within the meaning of the Act.

Counsel relied on three cases dealing with the difference between fixed and circulating capital: *Ammonia Soda Company, Limited* v. *Chamberlain* (1); *Atherton* v. *British Insulated and Helsby Cables, Limited* (2); *John Smith and Son* v. *Moore* (3).

A brief excerpt from the judgment of Lord Justice Swinfen Eady in the *Ammonia Soda Company, Limited* v. *Chamberlain* case seems to me proper (p. 286):

> The distinction between "fixed" capital and "circulating" capital is not to be found in any of the Companies Acts; it appears to have first found its way into the *Law Reports* in *Lee* v. *Neuchatel Asphalte Co.* (41 Ch. D. 1), where Lindley L.J. in his judgment adopted the expression which had been used by Sir Horace Davey in argument, derived from writers on political economy. It is necessary to consider the sense in which the expressions "fixed capital" and "circulating capital" were used in that case and in *Verner's Case* (1894, 2 Ch. 239). What is fixed capital? That which a company retains, in the shape of assets upon which the subscribed capital has been expended, and which assets either themselves produce income, independent of any further action by the company, or being retained by the company are made use of to produce income or gain profits. A trust company formed to acquire and hold stocks, shares, and securities, and from time to time to divide the dividends and income arising therefrom, is an instance of the former. A manufacturing company acquiring or erecting works with machinery and plant is an instance of the latter. In these cases the capital is fixed in the sense of being invested in assets intended to be retained by the company more or less permanently and used in producing an income. What is circulating capital? It is a portion of the subscribed capital of the company intended to be used by being temporarily parted with and circulated in business, in the form of money, goods or other assets, and which, or the proceeds of which, are intended to return to the company with an increment, and are intended to be used again and again, and to always return with some accretion. Thus the capital with which a trader buys goods circulates; he parts with it, and with the goods bought by it, intending to receive it back again with profit arising from the resale of the goods. A banker lending money to a customer parts with his money, and thus circulates it, hoping and intending to receive it back with interest. He retains, more or less permanently, bank premises in which the money invested becomes fixed capital. It must not, however, be assumed that the division into which capital thus falls is permanent. The language is merely used to describe the purpose to which it is for the time being appropriated.

(1) (1918) L.R. Ch. Div. 266.
(2) (1925) 1 K.B. 421.
(3) (1921) 2 A.C. 13.

At this point of the quotation counsel for appellant submitted that if the purpose is part of the scheme for profit making the capital is what is known as circulating capital.

Lord Justice Swinfen Eady goes on to say:

> This purpose may be changed as often as considered desirable, and as the constitution of the bank may allow. Thus bank premises may be sold, and conversely the money used as circulating capital may be expended in acquiring bank premises. The terms "fixed" and "circulating" are merely terms convenient for describing the purpose to which the capital is for the time being devoted when considering its position in respect to the profits available for dividend. Thus when circulating capital is expended in buying goods which are sold at a profit, or in buying raw materials from which goods are manufactured and sold at a profit, the amount so expended must be charged against, or deducted from, receipts before the amount of any profits can be arrived at. This is quite a truism, but it is necessary to bear it in mind when you are considering what part of current receipts are available for division as profit.

The same principle was adopted in the case of *Atherton* v. *British Insulated and Helsby Cables, Limited* hereinbefore cited. At page 440 of the report we find these comments in the reasons of Lord Justice Scrutton:

> The Attorney-General started with a definition of capital, which I hope I took down correctly. It was: "Any money expended upon a business which is intended to and does result in an asset is capital." The next time the Attorney-General on one side or the other of a revenue case formulates that definition I hope he will look at Swinfen Eady L.J.'s very careful description in the *Ammonia Soda Co.* v. *Chamberlain* (1918, 1 Ch. 266, 286) of the difference between "fixed" capital and "circulating" capital, because I think there is no doubt that circulating capital as defined by Swinfen Eady L.J. would not come within the terms of the Income Tax Act of money to be employed as capital, but it would come within the terms of the Attorney-General's definition. Without professing or intending for a moment to lay down a definition myself, having in my mind Lord Macnaghten's warning not to embarrass business men. I think it is clear that you must add to the words defining "asset" something to show that you are only speaking of assets in the nature of fixed capital. You expend your capital goods to get back a profit, but the fact that you expend the goods or buy the goods does not make the asset which results a capital asset, because it is not fixed capital, but is something which, in the language of Swinfen Eady L.J., is going to be circulated. I think, therefore, to get capital you must have some permanent extension of the business, which results in some sort of asset.

In the case of *John Smith and Son* v. *Moore,* on page 19 of the report *(in fine),* there is a brief comment by Viscount Haldane regarding the line of demarcation between fixed and circulating capital to which reference may be had beneficially.

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Counsel for appellant intimated that the principles applicable in deciding whether or not the profits made or the losses incurred in dealing with investments in securities must be regarded as capital losses or income losses have been clearly laid down but he admitted that the line of demarcation is sometimes difficult to draw, adding that one must confront the particular facts of each case with the principles expounded.

It was urged on behalf of appellant that in the present case we are faced with the task of deciding if the business which the company carried on in dealing with securities was a side of its business or a scheme for profit making and that the question will have to be decided on the basis of the evidence, which I may note is elementary, and having regard to the wide powers allotted to the company by its charter.

Counsel for appellant insisted on the fact that the company, in virtue of section 13 of its charter had the right to acquire, by purchase or otherwise, mortgages upon real estate, etc., with which we are not concerned, and bonds, debentures or capital stock of any incorporated company, and to resell the same. He drew a distinction between the powers given to the company by the first part of section 13 of its charter which, according to him, are not ordinarily allotted to a trust company and those provided for by the last part of the section, dealing with investments. It was contended on behalf of appellant that the power to invest offers no interest in the present case, because the company clearly has this power, which is inherent to every trust company.

Counsel for appellant asserted that his client has not actually carried on as a trust company, that it has not administered estates, but that it has acted as a company having on the one side clients' investments held in a trust account and on the other side its own funds used in the purchase of securities. He pointed out the course of trading exercised by the company, which is shown in the statement filed as exhibit 1 and upon which I do not think necessary to make further comments.

Counsel for appellant further pleaded that the transactions disclosed in the evidence were not done by the company for the purpose of nursing along its capital or

retaining it, but were done specifically with a view to realizing profits; that, in other words, the appellant was looking for ways and means of making the largest amount of money for its own benefit. He observed that during the course of its dealings the company purchased and sold many types of securities and that, if this had been done purely with the object of looking after its capital so that it would not lose it, the appellant would not have bought such a variety of securities, but would have invested its funds, as a trust company usually does, in safe securities, as preferred shares of the highest standard and not, to any large extent, in common stocks.

Counsel for appellant referred to *Plaxton (op. cit.)* with regard to the construction applicable to taxing statutes, where at page 5 the author says:

> In considering whether transactions bring the subject within the terms of the taxing Act, the substance rather than the form of the transaction is looked to.

In counsel's view there is no question, according to the evidence, that the substance of the transactions was that the company was engaged in them for the purpose of making a gain or profit and that for this reason they formed a part of the operations of the company's business.

Counsel concluded his remarks by stating that the case of the appellant is that it was given very wide powers by its charter and that pursuant thereto it purchased securities with a view to making a profit out of them. He submitted that subsequently it sold some of these securities and that, if it had sold them at a profit, the profit would have been subject to taxation. He added that in the present case the appellant, instead of selling at a profit, suffered a loss and that using the converse of the cases relied upon the company is entitled to deduct that loss for the purpose of ascertaining the net profit.

Before opening his argument counsel for respondent, Mr. Hollands, referred to the notice of dissatisfaction, particularly to paragraphs 2 and 3 in which the appellant sets forth "that for the taxation year 1936 the company's income tax return showed a profit made on the sale of bonds, which profit was included in its taxable income, and for which profit the company was assessed and paid income

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tax" and "that for the taxation year 1937 the company's income tax return showed a profit on the sale of bonds and a loss on the sale of real estate, both of which were accepted as proper by the taxing authority and were allowed, and the company was not assessed for income tax for that year". Counsel intimated that we are only interested in the assessment for the year 1941 and that, whether the Minister made a mistake, there having been no appeal in either year, the present case should be confined to the year 1941. I may say that I agree with counsel's submission, in spite of the fact that the Minister could unquestionably, as I think, have made a re-assessment in virtue of section 55 of the Income War Tax Act and that he did not see fit to do it.

It was urged by counsel that the name of the appellant company is a trust company and that a trust company is bound to have a capital stock to secure the clients dealing with it. He pointed out that under paragraph 3 of its charter the capital stock is fixed at one million dollars, divided into 10,000 shares of $100 each, and that it may be increased to a sum not exceeding two million dollars by a vote of two-thirds in number of the shareholders present or duly represented at any annual meeting or at a special meeting called for that purpose, provided that stock to the amount of $100,000 shall be subscribed and $35,000 paid thereon, before the company shall start operating.

Counsel stated that the objects of the capital did not appear to him to come within the purview of fixed or circulating profit. He added that the company could not perform its obligations unless it had this income.

Counsel observed that in virtue of section 4 of its charter the company has also the power to guarantee any investment made as agent or otherwise and "for and in respect of all or any of the services, duties or trusts hereinbefore (in the act of incorporation) mentioned, to charge and be allowed to collect and receive all proper remuneration and legal and other customary charges, costs and disbursements, with power to advance money to protect any such estate, trust or property entrusted to them . . . "

Reference was made to section 5, which gives to the appellant, among others, the power to act as executor and administrator. I may note that this is a power usually granted to a trust company.

It was argued by Mr. Hollands that section 13 is in the charter for the sole purpose of assisting the company in carrying out its trust agreements and that it is merely auxiliary to the company's main objects and purposes. Counsel intimated that what the appellant has done was not dealing in stocks, buying them and selling them with a view to making a profit, but in fact substituting securities. He pointed out that the purchases over a period of seventeen years totalled only thirty-three, while the sales numbered twenty-three. The least that can be said is that the appellant's business in dealing with stocks was surely not very active. From this state of affairs counsel concluded that the act of incorporation of the appellant limits it to a trust company business.

Counsel stated that a trust company is different from an ordinary company in that it cannot operate unless it has a foundation, which is its capital. He acknowledged that a trust company can substitute its capital for securities, adding that this is what the appellant did.

Mr. Hollands stressed the point that capital is not taxable and that consequently deductions cannot be allowed for any loss thereon.

He owned that he had no quarrel with the cases cited by his opponent, but said that the company was created as a trust company and that its capital was thereby intended to be fixed. He added that its capital is the foundation upon which rests its business, that it is not the business but is merely security to clients and the public so that they may have a recourse should the company fail in its duties.

Counsel referred to *Hatch* v. *Minister of National Revenue* (1). I do not think that this case has any bearing on the present issue.

Mr. McGrory, on behalf of respondent, stated that the Act of incorporation of the appellant enacts a trust company and that it would be a peculiar feature if the company did not have the power to acquire and sell securities, which

(1) (1938) Ex. C.R. 208.

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is a power inherent in every company, trust or otherwise. He thought that it is stretching the interpretation of section 13 of the charter, when read in conjunction with the whole Act, to say that the company was incorporated for the purpose of buying and selling securities, which, in his view, is merely an incidental power to invest its capital.

Mr. McGrory pointed out that, when asked the reason why the three sales of stocks which gave rise to the loss had been made, Woods replied that he did not know. On page 11 of his deposition we find in his answer previously quoted the following statement:

> But I can't tell you what prompted us in making these sales in that way.

Counsel suggested that it was a normal change of investment and for no particular reason other than an attractive investment to be made.

Counsel indicated that the stocks in which the appellant invested are all of the revenue bearing type and that everyone paid dividends during the taxation year 1941, even the three which were sold. According to him these stocks were held for investment by the company and any loss incurred in connection therewith would be a capital loss.

Mr. McGrory thought that the marginal note opposite section 13 of the charter: "Investment of Company's funds" is enlightening and that the whole tenor of the section points to a power to invest the company's funds.

In reply Mr. Smith urged that the marginal note opposite section 13 is not of great advantage because the section is definitely split into two parts and because this is where the appellant differs from an ordinary trust company. He emphasized the fact that the company is given two sets of powers, firstly to deal in securities and secondly to make investments. He repeated that the appellant does not carry on as a trust company and that it has given up the most lucrative business of such a company, to wit the administration of estates.

He agreed that a certain amount of capital had to be paid before the company could start in business, but said that what we are concerned with in the present case is

what the capital was used for. He intimated that the expression "fixed capital" has nothing to do with the fact that the amount of it may be fixed by statute. He expressed the opinion that counsel for respondent has misconceived the meaning of the expression "fixed capital", that it is not fixed in the sense that it is governed by statute, that the term has a technical meaning which is clear and that it applies to that portion of the capital of the company which is represented by fixed assets. He added that it is evident that there was a large revolving fund used for a number of purposes and that it cannot be considered as fixed capital. In his opinion the evidence discloses that, when the company bought securities, it looked to an appreciation in their value so that they would yield a profit.

He pointed out that in some of the cases cited it has been held that even isolated transactions may be taxable if they are part of the company's business. He concluded that the mere fact that the company may carry on several enterprises for the purpose of making money does not prevent a particular transaction from being taxable and that conversely under the authority of these cases, if losses are incurred, they are deductible for the purpose of ascertaining the net profit which is taxable.

The foregoing recapitulation of the evidence and argument is long but I thought advisable to give a complete history of the case.

The question arising for determination may be summed up as follows. Is the loss suffered by the appellant in the year 1941 on the sale of stocks and bonds amounting to $2,607.92 a loss of capital or a loss of profit incurred in the ordinary course of business? If it is the first it is not deductible from the gross profits. On the other hand, if it is a loss of profit it may be subtracted from the profits earned by the company during the year in question in order to establish the net taxable profit.

The evidence discloses that the appellant, although called a trust company, did not administer estates and did not act as executor. It dealt in mortgages, bonds and shares

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on its own account with a view to earning profits. It purported to make money through the increase in the market value of the securities purchased and resold at a profit.

In the taxing year 1941 the appellant sold the following securities:

Dominion of Canada bonds at a loss of	$ 12.50
Imperial Oil Company shares at a loss of	946.50
Canadian Northern Power Corporation Limited shares at a loss of	1,800.25
	$2,759.25
Carnegie Finance & Investment Company Limited shares at a profit of	151.33
Leaving a net loss of	$2,607.92

This appears in the deposition of J. D. Reid, auditor for the appellant company (pages 17 and 18).

After a careful perusal of the evidence and of the able and exhaustive argument of counsel and an attentive study of the law and the precedents I have reached the conclusion, with some hesitation I must admit, that the loss made by the appellant in 1941 was incurred in the ordinary course of its business as dealer in securities and that it must accordingly be considered as a loss of profit and not as a capital loss. In the circumstances I believe that the appellant was justified in deducting this loss from its profit for the year 1941. The appeal will consequently be maintained, the decision of the Minister set aside and the assessment declared unfounded, null and void.

The appellant will be entitled to its costs.

Judgment accordingly.