BETWEEN:

EDGELEY FARMS LIMITED ..... APPELLANT;

AND

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

Toronto
1968
Apr. 17-18

Income tax—Company formed to acquire land—Grant of long-term lease with option to buy—Profit from exercise of option and expropriation—Whether business profits.

Appellant company was incorporated in 1959 at the instance of four well-to-do men for the purpose of acquiring a 350-acre farm near Toronto as being a good buy though without any definite plan for realizing its potential value. Appellant operated the farm for a short time and then negotiated a 25-year lease of the land to an arm's length purchaser at a high rent subject to an option to purchase at a high price. In 1962 the lessee exercised the option on some of the land. In 1963 an additional part of the land was expropriated. Appellant made a profit of $23,375 on the 1962 sale and $3,100 on the 1963 expropriation.

Held, appellant was not taxable on these sums. Nothing in the circumstances displaced the conclusions that by granting the lease appellant

1968

EDGELEY FARMS LTD. v. MINISTER OF NATIONAL REVENUE

committed itself to holding the land as income-producing property for 25 years and that the option clause in the lease was not a dedication of the land to a trading operation.

M.N.R. v. Valclair Investment Co. [1964] Ex. C.R. 466; *M.N.R. v. Cosmos Inc.* [1964] Ex. C.R. 478, distinguished. *Regal Heights Ltd v. M.N.R.* [1960] Ex. C.R. 902, referred to.

INCOME TAX APPEAL.

Wolfe D. Goodman and *Arnold L. Cader* for appellant.

F. J. Dubrule and *J. M. Halley* for respondent.

JACKETT P. (orally):—This is an appeal from the appellant's assessment under Part I of the *Income Tax Act* for the 1962 and 1963 taxation years. What is involved for 1962 is a profit of $23,375 that the appellant made in that year by selling a part of an area of land that it had purchased in 1959. What is involved for 1963 is a profit of $3,100 that the appellant made as a result of an expropriation of another part of the same area of land. The appellant has been assessed on the basis that these amounts were profits from a "business" within the extended meaning of that word as used in the *Income Tax Act* and the sole question involved in the appeal is whether or not those amounts were properly so classified.

The appellant was incorporated in 1959 to acquire 350 acres of land pursuant to an arrangement that had already been worked out by the four individuals who caused it to be incorporated. The land stood in the apparent path of future development of Metropolitan Toronto and the land was acquired because the appellant's management were of the view that it was a good buy.

No attempt was made before me to support the contention put forward at earlier stages of the matter, and suggested in the notice of appeal to this court, that the property was acquired for the purpose of continuing the farming business carried on on the land by the previous owners.

Clearly, as I have said, the land was acquired because it was a good "buy". Its potential value was obvious. What the appellant would do with it was not decided at the time of acquisition. The incorporators were well to do and could afford to bide their time. What the appellant would do with

the land would depend on what opportunities presented themselves. I have no doubt that, if the guiding mind of the appellant were to have frankly answered questions at the time of acquisition, he would have agreed that the appellant might itself, at an appropriate time, erect on the land buildings suitable for the developing neighbourhood, with a view to renting them or selling them; he would also have agreed that, if the right opportunity or opportunities arose, the appellant might sell some or all of the property, and he would also have agreed that a really attractive bare land leasing proposal would receive careful consideration by the appellant. In other words, the land was not dedicated at the time of acquisition to any particular use. It might end up as stock-in-trade of a trading business or as the subject of a venture in the nature of trade. It might end up as the site for an income-producing building. It might end up as revenue-producing bare land.

In those circumstances, had the acquisition merely been followed by the 1962 sale, I should have had no doubt that the resultant profit was a profit from a business within the extended meaning of that word as used in the *Income Tax Act*. In effect, the appellant would have dedicated the land, or at least that part of it that it sold, to the carrying on of a trading business or a venture in the nature of trade. The two cases on which the appellant relied in that connection—*Minister of National Revenue v. Valclair Investment Co. Ltd.*[1] and *Minister of National Revenue v. Cosmos Inc.*[2] were decisions on different facts and do not do anything more than apply the ordinary principles that have been applied in a line of cases that are so well known that I need only refer to *Regal Heights Ltd. v. Minister of National Revenue*[3] as an example.

The facts are not, however, that simple. Having carried the farming business on for a short time and having then brought it to an end and liquidated the assets of that business other than the land, the appellant negotiated a twenty-five years lease at a very favourable rent with a person with whom it was dealing at arm's length. If the recital of the circumstances stopped there, I should not have had any

[1] [1964] Ex.C.R. 466.
[2] [1964] Ex.C.R. 478.
[3] [1960] S.C.R. 902.

1968

EDGELEY FARMS LTD. v. MINISTER OF NATIONAL REVENUE

Jackett P.

difficulty in concluding that, at least for the twenty-five year term of the lease, the appellant had dedicated the land to the role of an income-producing investment.

A further circumstance that created a difficulty in my mind, when I first tried to reach a conclusion as to how the particular profits should be classified, is that the long term lease contains an option clause under which the lessee is entitled, if it so elects, to purchase all or parts of the demised property at a price per acre that is substantially higher than the price paid by the appellant for the land. It was pursuant to this option clause that the appellant made the sale giving rise to the profit that is in issue for 1962.

While, as I say, this clause gave me trouble in trying to resolve the problem, I have not been able to find any basis on which I can use it as a reason for coming to a different conclusion than that that I would have reached if there had been a simple twenty-five year lease without an option clause. So far as the appellant is concerned, it has committed itself, by its demise to the lessee, to holding the land in question as income-producing land for twenty-five years. The option clause in no way constitutes a dedication of the land to a trading operation, nor does it confer on the appellant any means for disposing of the land within the twenty-five year period of the lease. Presumably, it was, as part of the process whereby the terms in the lease that were favourable to the appellant were obtained, that the lessee was granted the option clause.

From the point of view of the appellant's ability to sell the land free of the long term lease, the appellant was in the same position as though the lease contained no option clause. If there were no option clause, the appellant would not have been able to sell all or part of the land free of the lease without the cooperation of the lessee. The appellant was in exactly the same position with the option clause in the lease.

I cannot conceive that a similar option clause in a lease granted by a lessor who acquired land for the sole purpose of holding it for a rental income would turn his land holding operation into a trading "business". If it would not have such an effect in the case of such a person, I can conceive no

basis for holding that it would have that effect in the case of a person who acquired the land for an undetermined purpose and subsequently committed himself to holding it for rental under a long term lease.

The situation would have been different if the lease had been a mere device for dictating the terms of a land disposition operation. This might have been the case if the lease had been only part of a larger agreement between the appellant and the lessee. It might well have been a fair inference if the rent were so high in relation to the option price as to constitute a strong incentive for the lessee to exercise its option rights. Other circumstances, if they had existed, might have given rise to the same conclusion. No such circumstances had been assumed by the respondent as a basis for the assessments, or alleged by the respondent in his reply to the notice of appeal, and no such circumstance was put forward by counsel for the respondent in cross-examining the appellant's witness.

My conclusion is, therefore, that the land acquired by the appellant in 1959 was being held by the appellant in 1962 and 1963 for rental income under a long term lease, and that the sale in 1962 and the expropriation in 1963 did not give rise to profits from a "business" within the extended meaning of that word as used in the *Income Tax Act*.

The appeal will therefore be allowed and the assessments referred back to the respondent for re-assessment on the basis that the profits in question are not profits from a business. The appellant will have its costs of the appeal.