
THE MINISTER OF NATIONAL
REVENUE

APPELLANT;

1963
*May 10
May 10

AND

WILLIAM HEDLEY MACINNESRESPONDENT.

ON APPEAL FROM THE EXCHEQUER COURT OF CANADA

Taxation—Income tax—Mortgages purchased at a discount and held to maturity—Whether profits taxable income—Income War Tax Act, R.S.C. 1927, c. 97, s. 3—Income Tax Act, 1948 (Can.), c. 52, ss. 3 and 4—Income Tax Act, R.S.C. 1952, c. 148, ss. 3 and 4.

*PRESENT: Taschereau C.J. and Fauteux, Judson, Ritchie and Hall JJ.

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The respondent, an elderly businessman, was principally occupied as a soap manufacturer. Between 1944 and 1954 he purchased 309 mortgages at a discount from mortgages offered to him by various real estate agents. The mortgages so purchased were first mortgages but were regarded as substandard by mortgage companies; they were generally for amounts ranging from \$1,500 to \$3,000 and for a term of five to eight years. In the years 1946 to 1954 the respondent realized discounts on 113 of these mortgages which either matured or were paid off during that period. The discounts thus realized were assessed as income by the Minister. The Exchequer Court in dismissing an appeal from a judgment of the Tax Appeal Board held (a) that the discounts realized in the years 1946 to 1948 were not profits from a trade or business within s. 3 of the *Income War Tax Act*, and (b) that the discounts realized in the years 1949 to 1954 were not profits from a business within the meaning of that term as defined in the *Income Tax Act*. The Minister appealed to this Court.

Held: The appeal should be allowed.

It was quite impossible to distinguish this case, even on the facts, from those in *Scott v. Minister of National Revenue*, [1963] S.C.R. 223. The respondent was engaged in the highly speculative business of purchasing mortgages at a discount and holding them to maturity in order to realize the maximum amount of profit out of the transaction. The discounts realized by him were taxable income since they were profits or gains from a trade or business within the meaning of s. 3 of the *Income War Tax Act*, R.S.C. 1927, c. 97, and income from a business within the meaning of ss. 3 and 4 of the *Income Tax Act*, 1948 (Can.), c. 52, or ss. 3 and 4 of the *Income Tax Act*, R.S.C. 1952, c. 148.

Argue v. Minister of National Revenue, [1948] S.C.R. 467, distinguished.

APPEAL from a judgment of Thurlow J. of the Exchequer Court of Canada¹, affirming with a variation a judgment of the Tax Appeal Board. Appeal allowed.

D. S. Maxwell, Q.C., and *G. Ainslie*, for the appellant.

K. Eaton and *B. Crane*, for the respondent.

The judgment of the Court was delivered by

JUDSON J.:—The Minister of National Revenue appeals from the judgment of the Exchequer Court¹, which held (a) that certain discounts realized in the years 1946 to 1948 on the purchase of mortgages were not profits from a trade or business within s. 3 of the *Income War Tax Act*, and (b) that similar discounts realized in the years 1949 to 1954 were not profits from a business within the meaning of that term as defined in the *Income Tax Act*. It is the unanimous opinion of the Court that these receipts were taxable under the appropriate legislation.

As we are prepared on the facts, which are not disputed, to draw inferences different from those of the learned trial judge, it is necessary to state them in brief outline.

¹[1962] Ex. C.R. 385, [1962] C.T.C. 350, 62 D.T.C. 1208.

The Minister, in making the re-assessment for the taxation years under appeal, added to the respondent's income the following amounts in respect of discounts realized by the respondent on certain mortgages and agreements for sale which he had purchased. These realized discounts were:

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1946	\$ 750.00
1947	968.23
1948	1,523.17
1949	711.73
1950	1,397.00
1951	5,798.11
1952	8,212.72
1953	8,703.35
1954	10,667.67
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	\$ 38,731.98

At the time of the hearing of the appeal, the respondent was 83 years of age. He had had a long and varied business career. He had also held two offices in the Civil Service of the Province of British Columbia, one of which was that of Official Administrator for the County of Vancouver, which he held from 1925 to 1929. In the mid-thirties he went into the business of manufacturing soap and he was carrying on that business at the time of the appeal.

In 1944 the respondent began to purchase substandard mortgages at a discount. The following table shows by years the number of mortgages purchased at a discount between 1944 and 1954, and the aggregate of the amounts owing under the terms of the mortgages at the time they were acquired by the respondent:

<i>Year</i>	<i>Number</i>	<i>Purchase Price</i>	<i>Amount Owing</i>
1944	3	\$ 4,144.50	\$ 4,860.00
1945	1	914.00	975.00
1946	23	46,577.66	51,592.02
1947	25	50,169.83	62,529.97
1948	22	49,063.70	60,743.57
1949	30	72,096.06	85,423.63
1950	31	78,922.09	96,787.38
1951	36	89,790.68	115,802.80
1952	60	170,068.41	212,590.07
1953	34	115,835.07	148,365.76
1954	44	148,394.86	212,714.51
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	309	\$ 825,976.86	\$ 1,053,220.78 (*)

(*) The aggregate of the fourth column in the above table is, in fact, \$1,052,384.71, but the respondent conceded that the figure of \$1,053,220.78, arrived at by the appellant's assessors was the correct figure.

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Of the 309 mortgages acquired during the period between 1944 and 1954, 113 either matured or were paid off and the respondent realized discounts in the sum of \$38,731.98. In addition to these 113 mortgages, three or four additional mortgages in respect of which no discounts had been taken either matured or were paid off.

At the end of the respondent's 1954 taxation year, 196 of the 309 mortgages were still current and the amount of the unrealized discounts was \$171,000, and between 1954 and the date of the trial before the Exchequer Court, the bulk of the discounts in relation to these mortgages had been realized by the respondent.

Between 1954 and the date of the trial before the Exchequer Court, the respondent was still as actively engaged in obtaining further mortgages as he had been in the earlier years.

All of the mortgages which had been acquired at a discount were first mortgages but were regarded as substandard, since in most cases the principal amount secured represented up to two-thirds of the value of the property, instead of 45 per cent of the sale value which, according to the respondent's evidence, was the amount normally secured under a conventional first mortgage. It was the respondent's view that to the extent that the principal amount exceeded 45 per cent of the value of the property mortgaged, there was a "second mortgage factor" or a risk similar to that attaching to a second mortgage. All of the 309 mortgages acquired by the respondent were mortgages on which the principal repayable was in excess of 50 per cent of the value of the property mortgaged.

The sources of the funds with which the respondent acquired these mortgages were the profits from the soap business, the sale in the late forties and fifties of certain assets owned by him in Eastern Canada and the payments being received by him on the existing mortgages.

Most of the mortgages acquired by the respondent were mortgages on small old-fashioned houses with fir floors and old-fashioned plumbing, located in South Vancouver and Burnaby. The mortgages were generally for amounts ranging from \$1,500 to \$3,000 and for a term of five to eight years. They bore the current rate of interest payable on

first mortgages, and provided for monthly payments of between \$30 to \$45 per month on account of interest and principal.

Generally, the respondent, before acquiring a mortgage, would insist on the purchaser-mortgagor having an equity in the property equivalent to one-third of its value and would acquire these mortgages at a discount of 15 per cent.

The mortgages in question were all selected by the respondent from those offered to him by various real estate agents in whom he had reasonable confidence and who were constantly canvassing him to acquire these mortgages. Originally, the respondent purchased most of the mortgages from two real estate firms, but as time went on he dealt with up to ten or twelve real estate firms. Persons acting for vendors in the sale of property knew that the respondent was a person interested in purchasing substandard mortgages. The respondent never bargained over the amount of the discount; he either accepted or rejected the offer made by the real estate agent.

During the years in question, the respondent was principally occupied in carrying on his business as a soap manufacturer. However, he gave evidence to the effect that at all relevant times, the interest and discounts realized from the mortgages were as great as his profits from the soap business.

The learned trial judge found:

... In my view there is nothing in the case which characterizes what the respondent did as anything but mere investment of funds which he had available for investment.

... it would I think be unrealistic to look upon what he did as a course of conduct or scheme directed primarily to the making of profit by realizing such discounts. The interest return was of greater importance and the most that could be said on this score is that his object was to get both

... That these mortgages as a class were in fact good securities is demonstrated by the result and though each involved some risk and at that possibly a somewhat greater risk than the types in which the mortgage companies were interested, I see nothing so unusual about them as to suggest that the respondent chose them in the course of a gamble or adventure looking to the realization of a speculative profit.

In our opinion there was error in the judgment of the learned trial judge in failing to find on the evidence which I have outlined that the respondent had engaged in the highly speculative business of purchasing mortgages at a discount and holding them to maturity in order to realize

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the maximum amount of profit out of the transaction, and in failing to find that the discounts realized were taxable income since they were profits or gains from a trade or business within the meaning of s. 3 of the *Income War Tax Act*, R.S.C. 1927, c. 97, and income from a business within the meaning of ss. 3 and 4 of the *Income Tax Act*, 1948 (Can.), c. 52, or ss. 3 and 4 of the *Income Tax Act*, R.S.C. 1952, c. 148.

It is quite impossible to distinguish this case, even on the facts, from those in *Scott v. Minister of National Revenue*¹. We are also of the opinion that *Argue v. Minister of National Revenue*² is in no way relevant to the issues raised in the present appeal. The problem in *Argue* was whether what was admittedly interest earned on long-term real estate mortgages and agreements could be regarded as income derived from the carrying on of a money-lending business for the purposes of the *Excess Profits Tax Act*, 1940 (Can.), c. 32. There was no evidence in *Argue* that the mortgages acquired were risky securities and there was no issue raised concerning either discounts or bonuses. The Court was concerned exclusively with money paid to *Argue* as interest. The Court simply held that there was no evidence which would justify the finding that *Argue* was carrying on business as a money-lender—no evidence which would serve to convert what was admittedly interest received from securities into profits from a business.

The appeal should be allowed and the judgment of the Exchequer Court reversed with costs and the re-assessments referred back to the Minister in order to adjust the amount of the discounts realized and included in the respondent's income in accordance with the table of discounts set out above and totalling \$38,731.98, counsel having agreed upon these amounts.

Appeal allowed with costs.

Solicitor for the appellant: E. S. MacLatchy, Ottawa.

Solicitors for the respondent: Gowling, MacTavish, Osborne & Henderson, Ottawa.

¹ [1963] S.C.R. 223, [1963] C.T.C. 176, 63 D.T.C. 1121.

² [1948] S.C.R. 467, [1948] C.T.C. 235, 4 D.L.R. 161.