1968
*Oct. 16
1969
Jan. 28

J. HAROLD WOOD ..... APPELLANT;

AND

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

ON APPEAL FROM THE EXCHEQUER COURT OF CANADA

Taxation—Income tax—Income or capital gain—Mortgage acquired at a discount—Whether amount of discount collected at maturity income —Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 139(1)(e).

Between 1956 and 1963, the appellant, a solicitor, acquired eight first mortgages and five second mortgages, all but two of them at a discount. The appellant's investments were made entirely from savings not from borrowings, and his income from this source was a relatively modest part of his gross income. In 1962, he was assessed for income tax on $700, being the amount of a discount he collected on a mortgage acquired in 1957 and paid off in full at maturity. The Tax Appeal Board upheld the assessment. The Exchequer Court found that it "was income from a source within the meaning of the opening words of s. 3 of the *Income Tax Act*". The appellant was granted leave to appeal to this Court, where the issue was as to whether the discount was a profit from a business or adventure in the nature of trade by virtue of s. 139(1)(e) of the Act or whether it was a capital gain.

Held: The appeal should be allowed.

The amount received in 1962 represented a capital gain and not taxable income. The appellant's purchases were made entirely from savings, were not speculative and were made after inspection of each property. This pattern of activities was consistent with the making of personal investments out of savings and not with the carrying on of a business.

Revenu—Impôt sur le revenu—Revenu ou gain en capital—Hypothèque acquise à escompte—Le montant de l'escompte perçu à l'échéance est-il un revenu—Loi de l'impôt sur le revenu, S.R.C. 1952, c. 148, art. 3, 139(1)(e).

Durant les années 1956 à 1963, l'appelant, un avocat, a acquis huit premières hypothèques et cinq secondes hypothèques. Elles ont été acquises à escompte à l'exception de deux. Les placements de l'appelant provenaient de ses économies et non pas d'emprunts, et son revenu de cette source formait une faible partie de son revenu total. En 1962, le Ministre a cotisé l'appelant pour impôt sur le revenu sur $700, montant d'un escompte perçu d'une hypothèque acquise en 1957 et entièrement payée à l'échéance. La Commission d'appel de l'impôt a confirmé la cotisation. La Cour de l'Échiquier a statué que ce montant était un revenu d'une provenance dans le sens de ces mots au début de l'art. 3 de la *Loi de l'impôt sur le revenu*. L'appelant a obtenu la permission d'en appeler à cette Cour, où la question à

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*PRESENT: Abbott, Judson, Ritchie, Hall and Pigeon JJ.

déterminer était de savoir si l'escompte était un profit d'une entreprise ou d'une initiative d'un caractère commercial en vertu de l'art. 139(1)(*e*) de la Loi ou s'il s'agissait d'un gain en capital.

Arrêt: L'appel doit être accueilli.

Le montant reçu en 1962 représentait un gain en capital et non pas un revenu imposable. Les achats de l'appelant ont été faits entièrement à même ses économies, n'étaient pas spéculatifs et ont été faits après que l'appelant eut visité les lieux. Cette manière de procéder était compatible avec le placement personnel d'argents provenant d'économies et non compatible avec l'exploitation d'une entreprise.

APPEL d'un jugement du Juge Gibson de la Cour de l'Échiquier du Canada[1], en matière d'impôt sur le revenu. Appel accueilli.

APPEAL from a judgment of Gibson J. of the Exchequer Court of Canada[1], in an income tax matter. Appeal allowed.

F. Stewart Fisher, for the appellant.

G. W. Ainslie and *J. R. London,* for the respondent.

The judgment of the Court was delivered by

ABBOTT J.:—The appellant, a solicitor who has practised law in the City of Toronto since 1928, was at all material times a member of the firm Mackenzie, Wood & Goodchild. That firm had a general practice which included a "fairly substantial mortgage practice".

The firm, on behalf of clients, managed or supervised the collection of moneys lent on the security of mortgages and, between 1956 and 1963, the appellant had acquired personally an interest in thirteen mortgages. Eleven of these mortgages were acquired at a bonus or discount.

In July 1957, appellant, in association with a client, bought a first mortgage on which the amount then owing was $8,500 for principal, with interest at the rate of 6½ per cent per annum. The term of the mortgage was five years. Appellant and his client paid the sum of $7,100 each of them putting up one-half of the purchase price. The mortgage was paid off in full at maturity in July 1962.

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[1] [1967] 1 Ex. C.R. 199, [1967] C.T.C. 66, 67 D.T.C. 5045.

1969

WOOD
v.
MINISTER OF NATIONAL REVENUE

Abbott J.

Appellant was assessed for income tax in 1962 on $700 being his share of the discount on the said mortgage that he had collected in that year.

Before the Tax Appeal Board, the assessment was upheld on the finding, not that it was a profit from a business but that "it was a *quasi-bonus*", and therefore "interest *per se*".

In the Exchequer Court[2], Gibson J. did not wish to pass on the soundness of that conclusion and did not choose (those are his words) to make a finding that this was profit from a business. He expressly founded his decision on the basis that this "was income from a source within the meaning of the opening words of Section 3 of the *Income Tax Act*" adding:

> as far as I know there is no decision of this Court or of the Supreme Court of Canada in which a question of this kind has been resolved by deciding that such a discount was income from a "source" within the meaning of the opening words of s. 3 of the Act, without deciding whether it was income from any of the particular sources detailed in s. 3 or elsewhere in the Act.

From this judgment, appellant gave notice of appeal to this Court as of right, without apparently realizing that, due to the rate of tax payable, the actual amount in controversy was less than $500. Respondent also appears to have overlooked this point and did not move to quash but, on the contrary, signed an agreement as to the contents of the case and did not object to the appeal being inscribed for hearing. Before it came on for hearing, however, appellant applied for special leave to appeal and, in view of the importance of the question of law involved in the decision sought to be appealed from, leave to appeal was granted[3] by my brother Pigeon.

At the hearing before this Court, counsel for the Crown abandoned the contention that the payment of $700 received by appellant in 1962 was interest and conceded that the issue of the appeal turns upon a finding as to whether or not the said sum was profit from a business or adventure in the nature of trade by virtue of para. (*e*) of subs. 1 of s. 139 of the *Income Tax Act*.

Although certain specified receipts are declared to be income for the purposes of the Act, the *Income Tax Act*

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[2] [1967] 1 Ex. C.R. 199, [1967] C.T.C. 66, 67 D.T.C. 5045.

[3] [1968] S.C.R. 957, [1968] C.T.C. 446, 68 D.T.C. 5291.

does not purport to define income, it simply describes it. Section 3 mentions the three main sources of income (1) business (2) property and (3) offices and employment, but without restricting the general meaning of income as being income from all sources.

The task of determining the meaning of income for income tax purposes has been left to the courts. The English courts, whose decisions on this point the Canadian courts tend to follow, have determined the meaning of income for tax purposes without reliance upon economic theory. Income is to be understoood in its plain ordinary sense and given its natural meaning.

Since income tax is levied on an annual basis and capital gains are not included in income for tax purposes, it is necessary to determine whether a particular receipt, in a particular taxation year, is an income receipt or a capital receipt. In the case of a mortgage discount, such as the one in issue in this appeal, it is now well settled that the answer to that question depends upon whether the amount received should be classified as income from a business or as an accretion to capital.

In *Scott v. Minister of National Revenue*[4], Judson J., after reviewing a line of cases in the Exchequer Court dealing with this problem, in some of which it was held that the taxpayer was engaged in investment, and in others in a scheme for profit-making, said at p. 225:

> This diversity of opinion is understandable when the decision must depend upon a full review of the facts in each case for the purpose of determining whether the discounts can be classified as income from a business. Even on the same facts, there is room for disagreement among judges on the conclusions that should be drawn from these activities of a taxpayer, for the Act nowhere specifically deals with these discounts, as it does, for example, in s. 105 (*a*) with shares redeemed or acquired by a corporation at a premium. It is possible to deal expressly with the problem and the Act had not done so.

The appellant's investments, including investments in mortgages, were made entirely from savings not from borrowings, and his income from this source, including income from stocks and bonds, was a relatively modest part of his gross income. During the period from 1956 to 1963 inclusive, the appellant acquired eight first mortgages and

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[4] [1963] S.C.R. 223, [1963] C.T.C. 176, 63 D.T.C. 1121, 38 D.L.R. (2d) 346.

1969

WOOD v. MINISTER OF NATIONAL REVENUE

Abbott J.

five second mortgages all but two of them at a discount or bonus. This represents an average of one and one-half mortgages per year. The particulars of these mortgages are as follows:

1956 — 1 mortgage — $7,000
1957 — 1 mortgage — $7,100 (½ interest)
1958 — No mortgages
1959 — 1 mortgage — $2,500
1960 — 2 mortgages — $6,600
1961 — 4 mortgages — $22,412.20
1962 — 1 mortgage — $4,000.00 (no bonus or discount)
1963 — 3 mortgages — $17,000.00 (no bonus or discount)

As stated, appellant acquired his one-half interest in the mortgage in issue here in 1957, and it was the only acquisition in that year. Appellant's purchases were not speculative and, according to his evidence, they were made after he had inspected each property and reached a decision that each mortgage was a safe investment for him.

In my opinion, this pattern of appellant's activities was consistent with the making of personal investments out of his savings and not with the carrying on of a business. It follows that the amount of $700, received in 1962, represented a capital gain and not taxable income.

I would allow the appeal and direct that the assessement be referred back for reconsideration in accordance with these reasons. The appellant is entitled to his costs throughout.

Appeal allowed with costs.

Solicitors for the appellant: MacKenzie, Wood & Goodchild, Toronto.

Solicitor for the respondent: D. S. Maxwell, Ottawa.