TIP TOP TAILORS LIMITED .... APPELLANT; 1957 *Mar. 26, 27 Oct. 1

AND

THE MINISTER OF NATIONAL REVENUE .... RESPONDENT.

ON APPEAL FROM THE EXCHEQUER COURT OF CANADA

Taxation—Income tax—What is "profit from business"—Dealings in foreign exchange—The Income Tax Act, 1948 (Can.), c. 52, ss. 3, 4, 127(1)(e).

The appellant company bought large quantities of cloth in Great Britain. Before 1948, its practice was to pay for each lot by an individual purchase of sterling at the rate of exchange then prevailing. In January 1948 the officers of the company, foreseeing a possible devaluation of sterling, arranged with a bank in London for a line of credit to a stated maximum which could be called in by the bank at the end of each year. Thereafter, as each shipment of cloth was received the London bank was instructed to pay the seller and the price was entered in the company's books in Canadian dollars at the current rate of exchange. When the bank overdraft was paid in September 1949, the rate of exchange had dropped and the company thus made a net profit of $169,000.

Held (Cartwright J. dissenting): This profit was taxable as income of the company under the *Income Tax Act,* 1948.

Per Kerwin C.J. and Locke J.: In essence, there appeared to be no difference in the resulting profit whether it was expressed as one realized by the reduction in the number of Canadian dollars needed to discharge the debt to the bank or as a reduction in the cost to the taxpayer of the merchandise purchased and used during the period, and the profit that would have resulted had the taxpayer sold sterling short to the requisite amount. In either case, it was a profit made in one necessary part of the appellant's trading operations and was not a capital gain as a result of speculation in sterling. *Atlantic Sugar Refineries Limited v. The Minister of National Revenue,* [1949] S.C.R. 706; *Imperial Tobacco Co. (of Great Britain and Ireland) Ltd. v. Kelly* (1943), 25 Tax Cas. 292, applied; *McKinlay v. H. T. Jenkins and Son, Ltd.* (1926), 10 Tax Cas. 372, distinguished.

Per Rand and Fauteux JJ.: The profit was not to be regarded as one on a collateral borrowing of capital but rather as one derived from the "business" in which the company was engaged. The loan produced working capital used in the course of the company's business and in substance the creation of debt in the bank was merely a substitution of creditor for the actual transactions. There was no temporary investment in foreign capital.

Per Cartwright J., *dissenting*: There was nothing in the evidence sufficient to displace the *prima facie* presumption that a saving made in discharging an obligation to a lender was properly treated as an item of capital and not of revenue. Applying that presumption to this case, the profit was not taxable.

---

*PRESENT: Kerwin C.J. and Rand, Locke, Cartwright and Fauteux JJ.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

APPEAL from a judgment of Cameron J. of the Exchequer Court of Canada (1), reversing a judgment of the Income Tax Appeal Board (2). Appeal dismissed.

Lazarus Phillips, Q.C., and *Philip F. Vineberg,* for the appellant.

D. W. Mundell, Q.C., and *R. A. P. Montgomery,* for the respondent.

The judgment of Kerwin C.J. and Locke J. was delivered by

LOCKE J.:—The *Income Tax Act,* 1948 (Can.), c. 52, does not contain any further definition of "income" which requires consideration in this case than that to be found in ss. 3 and 4. In this respect it differs from its predecessor, the *Income War Tax Act,* R.S.C. 1927, c. 97, where the meaning to be assigned to the term in the Act was elaborately defined.

Section 3 of the 1948 Act says that the income of a taxpayer for a taxation year for the purposes of Part I of the Act is his income from all sources inside or outside Canada and without restricting the generality of the foregoing includes income from, *inter alia,* all businesses. Section 4 so far as it is relevant merely says that income for a taxation year from a business is the profit therefrom for the year. Accordingly the only question to be considered is whether the profit which was undoubtedly realized in the present matter is a profit from the business carried on by the appellant.

The relevant facts are detailed in the judgment of Cameron J. delivered in the Exchequer Court (1). The purpose of the borrowing from the Canadian Bank of Commerce branch in London was stated during cross-examination of the witness Clayton, the secretary and controller of the appellant company, in these terms:

> . . . it was felt that the pound sterling would be devalued, and after discussing the matter fully with the president and other top officials in the company we decided to deliberately pursue this policy of running a large overdraft in England in the hope of gaining the capital profit on devaluation.

(1) [1955] Ex. C.R. 144, [1955] C.T.C. 113, 55 D.T.C. 1083.

(2) *Sub nom. No. 137 v. Minister of National Revenue* (1954), 9 Tax A.B.C. 377, 54 D.T.C. 23.

1957

TIP TOP TAILORS LTD. *v.* MINISTER OF NATIONAL REVENUE

Locke J.

And again:

> I contend that that profit is the result of a premeditated act on my part and other officials of the company to build up a liability in England when, in fact, we could have specifically paid out of funds that we had in Canada, and it had no relationship whatsoever with the merchandise, as you are saying it does, in that once we paid a supplier the transaction was completed with the supplier and we had no more recourse to him. In normal circumstances, for as long back as I can trace the records, the procedure was different, and it was only during this 18 months when we tried to go short of sterling and the procedure was different and resulted in a capital profit, and has no relationship, in my opinion, to the merchandise.

While the foregoing is rather more argument than a statement of facts it makes clear the purpose of the course that was followed. The question as to whether the gain made by the company is a capital profit is, of course, the point in the case.

It is, in my view, of importance to note that while, as Clayton's evidence indicated, the appellant intended to advance the claim that any profit realized as a result of devaluation of the pound was a capital gain resulting from what was to be a speculation in foreign exchange, the interest charges on the bank loan were charged in the years 1948 and 1949 as expenses of the operation of the business. In my opinion the present matter is concluded against the appellant by the decision of this Court in *Atlantic Sugar Refineries Limited v. The Minister of National Revenue* (1). I am unable to differentiate the position of the taxpayer in that case in respect of the profit made on the short sales of sugar from the position of the appellant in regard to the profit that was made due to the fall in value of the pound.

At the commencement of the year 1948 the appellant had a very small overdraft with the bank in London and from then until September 1949 it used sterling borrowed from that bank to pay for the goods used in its manufacturing operations in Canada. The purpose of incurring the overdraft was made clear by Clayton. It was the hope that when it became necessary to pay the overdraft the value of the pound in relation to the Canadian dollar would have dropped, the practical result of which would be that the cost of the goods which had been used in the operations or purchased during that period would be reduced. In essence

(1) [1949] S.C.R. 706, [1949] C.T.C. 196, [1949] 3 D.L.R. 641.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

Locke J.

there appears to be no difference between the resulting profit, whether it be expressed as one realized by the reduction in the number of Canadian dollars needed to discharge a debt or as a reduction in the cost to the taxpayer of the merchandise which had been used and purchased during the period, and that which would have resulted had the taxpayer sold sterling short to the requisite amount.

I agree with the learned trial judge that it was a scheme for profit-making in one necessary part of the appellant's trading operations, namely, the purchase of sterling funds and part of an integrated commercial operation being the purchase of the supplies and the payment for them in that currency. It was apparently treated as such in the preparation of the appellant's accounts for the years in question since if it was simply a speculation in sterling exchange divorced from the company's trading operations the interest payable on the bank loan would not have been deductible as an operating expense.

In my opinion the decision of Rowlatt J. in *McKinlay v. H. T. Jenkins and Son, Limited* (1) does not assist the appellant. As the report of that case indicates, Rowlatt J. treated the purchase of Italian currency which was made as an investment into which the taxpayer had put its money temporarily. The learned judge explained the ground of his decision in *McKinlay's Case* in the case of *George Thompson & Co., Ltd. v. The Commissioners of Inland Revenue* (2) where he said that he had considered that it was a case where they had some capital lying idle and they embarked upon an exchange speculation.

This fact is commented upon by Lord Greene M.R. in delivering the judgment of the Court of Appeal in *Imperial Tobacco Co. (of Great Britain and Ireland), Ltd. v. Kelly* (3), where, however, it is pointed out that the case stated in *McKinlay's Case* does not appear to contain any basis for a finding that the original purchase of the lire was a speculation. There had been, however, no appeal from the decision of Rowlatt J. and Lord Greene did not further express his opinion as to its accuracy.

(1) (1926), 10 Tax Cas. 372.

(2) (1927), 12 Tax Cas. 1091 at 1102.

(3) 25 Tax Cas. 292 at 301, [1943] 2 All E.R. 119 at 122.

Decisions as to what constitutes "income" under sched. D of the *Income Tax Act,* 1918 (U.K.), c. 40, appear to me to be of value in considering cases such as the present arising under the statute of 1948. To what extent they touch such cases arising under the *Income War Tax Act* need not here be considered. Under sched. D, s. 1, the tax is applied to the annual profit or gains arising, *inter alia,* from any trade whether the same be carried on in the United Kingdom or elsewhere. This does not appear to differ from ss. 3 and 4 of the Canadian statute.

In the *Imperial Tobacco* case the company carrying on business in England had acquired a large amount of American exchange for the purchase of tobacco in the United States and when the American dollars were requisitioned by the treasury in England they had appreciated greatly in value in terms of sterling. The question was as to whether the resulting profit to the company was income. Lord Greene said in part (1), after referring to *Thompson's* case:

> In the present case it is truly said that it was no part of the company's business to buy and sell dollars. But in each case the commodity (in the one case the coal and in the other case the dollars) was required for the purpose of transactions on revenue account and nothing else.

and held the profit to be taxable income. In the present matter the borrowings of sterling from the bank were made for the purpose of transactions on revenue account to the same extent.

The decision in *Tax Case No. 308* (2) does not, in my opinion, assist the appellant. That matter was decided in a special Court for hearing income tax appeals, the judgment being delivered by the learned President. The report contains a very meagre statement of the facts but it appears that the taxpayer, which carried on business in South Africa, had for many years financed its obligations by an overdraft in London. When the United Kingdom left the gold standard, the company took advantage of the favourable rate of exchange which resulted to discharge its liability on the overdraft for an amount in South African pounds substantially less than the nominal amount of its debts expressed in sterling. The profit thus resulting was held to

(1) 25 Tax Cas. at p. 301. (2) (1934), 8 S.A. Tax Cas. 99.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

Locke J.

be a capital gain on the ground that the debt due to the bank on overdraft was of the nature of a loan and, therefore, a capital liability.

The report does not contain the statutory definition of income in the statute which affected the matter and the evidence did not disclose the purpose for which the moneys borrowed had been disbursed. It was, apparently, on the ground that the borrowing of money is *prima facie* a liability on capital account that, in the absence of other evidence, the learned President considered that the profit was a capital gain.

I see no relation between this set of facts and the present, where the exact purpose for which the moneys were borrowed from the bank was as above stated, being for the purpose of transactions on revenue account and nothing else, to adopt the language of the Master of the Rolls in the *Imperial Tobacco* case.

Everything that could be fairly urged on behalf of the appellant in the present matter has been said by the learned counsel who appeared on its behalf but, in my opinion, this appeal should fail for the above reasons.

The judgment of Rand and Fauteux JJ. was delivered by

RAND J.:—The appellant company deals in large-scale manufacture of wearing apparel in the course of which quantities of cloth are purchased in lots from Great Britain. Its ordinary practice, prior to January 1948, was to pay for each lot according to the terms of the invoice by an individual purchase of sterling at the rate of exchange then prevailing. In that month the officers of the company, foreseeing the likelihood of a devaluation of sterling, made preparations to avail themselves of the benefit of that happening should it eventuate.

The company thereupon arranged with a Canadian bank having a branch office in London for a line of credit at that office to a maximum of £250,000 which could be called in by the bank at the end of each year. Although this credit may have been available for any purposes of the company, that it would be resorted to for some or all of its purchases of material for its business is quite evident, and no other purpose is suggested. The debit account accumulated until September 1949; interim payments during that period were from time to time made on the loan generally for the purpose of keeping it within what were considered to be desirable limits. In that month the pound was devalued and the amount then reached, approximately \$588,000, was, in the course of weeks, liquidated by purchases of sterling at the lower rate.

During this period of approximately twenty months the purchases of goods were settled in the following manner: when the goods had been received in Canada, and within the terms of the invoice, a direction would be forwarded to the bank in London to make payment to the seller; at the same time the price would be entered in the books of the company in Canadian dollars at the then officially fixed rate of exchange; and when payment was made the purchase became a closed transaction. The total outstanding advances in September 1949, cleared at the lower rate, consisted solely of accumulated sums paid in this manner to sellers of cloth, *i.e.*, goods bought by the company in the course of its trade. Up to devaluation the rate was \$4.04 to the pound but the bank overdraft was paid on an exchange rate of \$3.0875. The net profit was approximately \$160,000 and the question is whether that profit is taxable as income.

The company's contention is that the profit was on a collateral borrowing of capital, a single and discrete transaction, not in the course of any business carried on by it, in effect, a temporary capital investment in foreign currency. As a profit on such an investment it is not within the scope of the taxing statute.

The Crown's answer is that this mode of financing was, as created, an inseparable part of and merged in the business in which the company was engaged; or if not, that it was a venture within s. 127(1)(*e*) of the *Income Tax Act,* 1948 (Can.), c. 52, which defines "business" as including "an adventure or concern in the nature of trade".

A number of authorities were examined by both counsel which bear more or less directly upon dealings involving foreign exchange. Those relied on by the Crown were cases in which the exchange was encountered as part of the transaction of purchase and sale as between the buyer and seller themselves: the exchange benefit or detriment was immediately involved in the actual payment to the seller of the

1957
TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE
Rand J.

price of goods purchased. Admittedly in such a mode of dealing the rate of exchange at the time of payment and not at any other time controls: the actual outlay by the purchaser to the seller for the goods received, in terms of the domestic currency, is the amount which must be taken into the account.

Between that and the practice here there is, no doubt, a difference in fact. When the goods were paid for with the borrowed sterling, the relation between buyer and seller, for those goods, was ended. Entry had to be made in various records, in London between the bank and the purchaser, in Canada between the purchaser and seller. What remained outstanding was the debt to the bank owing by the purchaser, and with this transaction the seller had nothing to do.

The proposition that the risk of a change in value of capital securities or investments is that of capital can be accepted. The capital machinery within and by means of which the business earning the income is carried on is distinct from that business itself; and the fluctuations in its value have no bearing on profits or losses from the business.

That distinction was stated with clarity by Lord Macmillan in *Montreal Coke and Manufacturing Company v. Minister of National Revenue; Montreal Light, Heat and Power Consolidated v. Same* (1). At p. 134, he puts it thus:

> It is not the business of either of the appellants to engage in financial operations. The nature of their businesses is sufficiently indicated by their titles. It is to those businesses that they look for their earnings. Of course, like other business people, they must have capital to enable them to conduct their enterprises, but their financial arrangements are quite distinct from the activities by which they earn their income. No doubt, the way in which they finance their businesses will, or may, reflect itself favourably or unfavourably in their annual accounts, but expenditure incurred in relation to the financing of their businesses is not, in their Lordships' opinion, expenditure incurred in the earning of their income within the statutory meaning. The statute, in s. 5(*b*), significantly employs the expression "capital used in the business to earn the income" differentiating between the provision of capital and the process of earning profits.

The principle was applied by this Court in *Bennett and White Construction Company Limited v. The Minister of National Revenue* (2), in which certain payments, made

(1) [1944] A.C. 126, [1944] 1 All E.R. 743, [1944] 3 D.L.R. 545.
(2) [1949] S.C.R. 287, [1949] C.T.C. 1, [1948] 4 D.L.R. 817.

as the price of obtaining guarantees required for bank advances to the company, were held to be of a capital nature and not deductible.

An analogous application was made in *McKinlay v. H. T. Jenkins and Son, Limited* (1). A contractor, undertaking work which called for the use of Italian granite, purchased lire in advance of his requirements. The exchange value of the lira went up, the contractor sold at a profit and later repurchased when the value had fallen off. The gain was held to result from an isolated transaction in a capital dealing and was not income. In the language of Rowlatt J. the profit was not "connected with the contract to construct"; it was an appreciation of a temporary investment, a dealing not merged in the business. So, too, in *Davies v. The Shell Company of China, Limited* (2). There the company sold petroleum products in China to agents who paid as the products were sold. To secure the seller's position the agents were required to deposit sums in Chinese dollars with the seller. The latter transferred the deposits to London and converted them into sterling. Three years later, when the business in China was brought to a close, the amounts due the agents in Chinese currency were repaid them. The value of that currency had declined and the company realized a substantial benefit in pounds sterling, which was held not to be taxable income.

The dealings before us are not, in my opinion, within that differentiating conception. The loan produced working capital used in the course of the company's business; the loan was effected as each payment was made to a seller; but in substance the creation of debt in the bank was merely a substitution of creditor for the actual transactions: no advance was ever made or, so far as the case goes, was ever agreed to be made to the company itself. Mr. Phillips, in his plausible argument, stressed the arrangement as a temporary investment in foreign currency. But what, in the sense of *McKinlay*, is an investment? Surely it involves the putting at risk by the investor of an asset or interest of value from which an increment of additional return of value is ordinarily hoped for. Here there was simply an accumulation of debt as the transactions of the business proceeded. No asset was put at risk by the company: the obligation of

(1) (1926), 10 Tax Cas. 372. (2) (1951), 32 Tax Cas. 133.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

Rand J.

the bank was to pay the sellers of the goods and them only. Even the elements here of a short sale of sterling do not, as a collateral investment, bring it within the meaning of *McKinlay*. What was intended and done was the creation of indebtedness to the bank arising directly out of the business and we cannot distort that into a purchase from the bank and a payment, as a matter of choice, by the company to the supplier: actual sterling as a commodity never existed in the ownership of the company. The only difference between that course of dealing and the ordinary monthly arrangements with a bank lies in the possibly greater time allowed the outgoings to accumulate. It was a large scale process of overdraft through a substantial period of time which I am quite unable to view as an investment.

From South Africa, *Income Tax Case No. 308* (1) was cited as a direct authority for the company. There the taxpayer, carrying on business in South Africa, had for many years financed its many operations by an overdraft with a bank in London. When the United Kingdom left the gold standard the company discharged the overdraft at a favourable rate of exchange, and the question, as here, was whether that gain was of an income or capital nature. In the circumstances it was held to be of the latter, but in the reasons the following language, at p. 100, clearly differentiates the case from that before us:

> Now, it seems to us, having regard to ordinary business and banking experience, that it would be absolutely impossible to dissect the various items in an overdraft account. Mr. Aiken has frankly admitted that his client, the appellant company, could not possibly trace each item in the overdraft and show whether it was applied or not to the discharge of trading liabilities. The appellant company has been carrying on a system of overdraft transactions with the bank for many years past, and it may very well be that certain items went to the discharge of trading liabilities, while other items may not have been applied to such liabilities. All we know is that this money went to the discharge of this overdraft. It would be quite impossible, as I have said, to dissect these various payments more especially as an overdraft goes up and down, and is decreased by other payment made from time to time, while it is swollen by further borrowings which are made by the client of the bank; but for all ordinary purposes an overdraft is a borrowing of money.

What was impossible there is admitted here: the accumulated debt was exclusively that of payments made in the course of the trade; and that circumstance is itself sufficient to distinguish the cases and to justify the difference in their ultimate determination.

(1) (1934), 8 S.A. Tax Cas. 99.

The dealings here are, I think, governed by a decision of the Court of Appeal of England, *Imperial Tobacco Co. (of Great Britain and Ireland), Ltd. v. Kelly* (1). The tobacco company, an English incorporation, was a buyer of large quantities of tobacco leaf in the United States. During the first months of 1939, in preparation for that year's purchasing in the late summer and early autumn, the company bought $45,000,000 at rates of exchange varying between $4.63 and $4.68 and the money was remitted to the United States to be used to buy the ensuing year's stock. On September 3 the war with Germany broke out and on the 8th of that month the British Treasury requested the company to stop all further purchases. As a result of compliance, there remained of the American currency unusable approximately $25,755,000. On September 30 the British treasury required the company to sell this surplus of dollars to it. Owing to the rise in the dollar exchange which had occurred, the price received by the company was much larger than that paid and the difference was included in the computation of taxable profits. It was held by Macnaghten J. and by the Court of Appeal that the gain was attributable to the business carried on by the company. Lord Greene M.R., with whom MacKinnon L.J. and du Parcq L.J. concurred, took the view that the acquisition of the dollars was simply the first step in carrying out the purchases of the leaf and the payment of its price. Bought for that purpose, the currency took on a revenue characteristic which was not lost when the surplus was sold. The argument against that seems to have been directed mainly to the circumstance that the disposal was not voluntary but dictated by the Treasury and a considerable part of the reasoning was to meet that consideration. *McKinlay's Case, supra,* was examined and distinguished.

The principle there followed, however sound its application, and I do not imply a doubt of that, is, *a fortiori,* appropriate here. Every dollar of the accumulated debt represents the discharge of purchase-price of goods bought. From the standpoint of investment, that case is much clearer; the exchange was bought generally and that allocated to the specific purchases was chargeable at the exchange existing at the moment of purchase. In both

(1) 25 Tax Cas. 292 at 293, [1943] 2 All E.R. 119.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

Rand J.

cases the foreign currency was used in the purchase of a commodity for the company's trade, but in that before us, the sterling representing the debt had no existence apart from that use.

Mr. Phillips urged the analogy of a loan by way of bonds or debentures repayable, say, in 1 or 2 years. If the money was raised for the purpose and used as here, that is, for and as working capital that was immediately employed in the course of the company's business, there would not seem to be any difference, and profit realized upon the redemption of the bonds or debentures might find itself gathered into income. It is difficult to distinguish a liability represented by bonds or debentures for a short period and mere indebtedness however represented when the character of the money and the purpose of its employment are the same. Bonds or other securities representing permanent or fixed features of the capital structure are entirely different in their nature and incidents.

Mr. Phillips also stressed the distinction between sterling as a commodity and as a medium of exchange, but, as already remarked, here no sterling was ever owned by the company as a commodity. A contractual right, assuming that the arrangement went so far, to have a bank pay bills on behalf of a purchaser as they are presented by sellers of goods, does not entail a purchase of a commodity for the company; and it is confusing the issue to speak of the arrangement as having produced a temporary investment: a debt is neither an asset nor an investment of the debtor, even though, as here, it may be exposed to the risk of variable value in terms of a foreign currency.

It follows that the appeal must be dismissed with costs.

CARTWRIGHT J. (*dissenting*):—The relevant facts out of which this appeal arises are undisputed.

The appellant has for many years carried on the business of manufacturing and selling clothing and in the course of that business makes large purchases of woollens in the United Kingdom the price of which is payable in sterling. For some years prior to January 1948 its practice was to purchase the necessary sterling funds to pay for each lot of goods bought but at about the date mentioned it arranged to borrow sterling from a bank in England. The funds borrowed were used to pay the vendors of the goods purchased and the cost of each lot of goods was charged in the appellant's books in dollars at the current rate of exchange which had for some time been pegged at $4.04 to the pound. Admittedly this arrangement was made in the expectation that the pound would be devalued and that a substantial saving to the appellant would result.

On September 20, 1949, the rate of exchange was altered to $3.0875. At this date the appellant owed the bank in round figures £178,000. In October 1949 the appellant paid off this indebtedness at the new rate of exchange. The amount in dollars required to make this payment was less by $169,614.96 than it would have been at the old rate. The respondent in assessing the appellant for the year 1949 added this sum to its declared income. The item in the notice of assessment reads:

Add: Profit on Foreign Exchange $169,614.96

The appellant's appeal to the Income Tax Appeal Board was allowed and the assessment referred back to the Minister for reassessment by deleting the amount in question from the taxable income (1). An appeal by the respondent to the Exchequer Court was allowed and the assessment affirmed (2). From that judgment this appeal is brought.

The gist of the decision of the Income Tax Appeal Board, delivered by Mr. W. S. Fisher, Q.C., is contained in the following paragraph (3) in his reasons:

> In the case of a debenture or bond issue floated by a company and subsequently liquidated or paid off for a smaller amount than that originally received, I am of the opinion that the difference would have been treated as a capital profit without question, and that this would be so even although the proceeds of the debenture or bond issue had been used in the business of the company for the purchase of raw materials utilized in the company's manufacturing and trading operations. In my opinion, the loan obtained from the British bank was borrowed capital, and when that loan was repaid by the appellant, the profit realized was a capital profit which was not subject to income tax under the Act. The profit in question did not arise out of the trading operations of the appellant company. The goods which it purchased in Great Britain were paid for promptly by it within a very short time after the goods were delivered, and the transaction was then closed. The fact that the payment was made

(1) *Sub nom. No. 137 v. Minister of National Revenue* (1954), 9 Tax A.B.C. 377, 54 D.T.C. 23.

(2) [1955] Ex. C.R. 144, [1955] C.T.C. 113, 55 D.T.C. 1083.

(3) 9 Tax A.B.C. at p. 379.

1957

TIP TOP TAILORS LTD. v. MINISTER OF NATIONAL REVENUE

Cartwright J.

out of monies borrowed from a bank does not, in my view, bring the bank loan into the category of ordinary day-to-day transactions carried on by the company. At all times, the position of the appellant in relation to the British bank was that of borrower to lender, and it was not part of the business of the appellant to deal in foreign exchange.

In the Exchequer Court, Cameron J. after a careful review of a number of authorities reached the conclusion (1) "that the profit made in the instant case was one made in the ordinary course of the respondent's business operations and while engaged therein on a scheme for profit-making".

After considering all of the decisions referred to in the reasons of Cameron J. and those discussed by counsel in the argument before us, it is my opinion that, in the case of a taxpayer carrying on a commercial undertaking such as that of the appellant, whose business is not that of dealing in foreign exchange or borrowing and lending money, a gain or loss related to dealings between borrower and lender is *prima facie* one of capital and not of income. This appears to me to be the result of the decisions in *Davies v. The Shell Company of China, Ltd.* (2), *Montreal Coke and Manufacturing Co. v. Minister of National Revenue; Montreal Light, Heat and Power Consolidated v. Same* (3), and *Bennett and White Construction Company Limited v. The Minister of National Revenue* (4).

In the case at bar I can find nothing sufficient to displace this *prima facie* presumption that a saving made in discharging an obligation to a lender is properly treated as an item of capital and not of revenue. The circumstance that the payments of interest to the bank were charged as expenses of the operation of the appellant's business in the years 1948 and 1949 does not appear to me to assist the respondent. The money borrowed was used as part of the appellant's working capital and the interest was "an amount paid in the year . . . pursuant to a legal obligation to pay interest on borrowed money used for the purpose of earning income from a business" and was properly deductible from taxable income under clause (*c*) of s. 11 (1) of the *Income Tax Act*, 1948 (Can.), c. 52.

(1) [1955] Ex. C.R. at p. 155.

(2) (1951), 32 Tax Cas. 133.

(3) [1944] A.C. 126, [1944] 1 All E.R. 743, [1944] 3 D.L.R. 545.

(4) [1949] S.C.R. 287, [1949] C.T.C. 1, [1948] 4 D.L.R. 817.

I think I am right in saying that in none of the cases relied upon by the respondent was a profit held to be taxable which arose in dealings where the relationship between the parties was solely that of lender and borrower. For this reason I do not propose to deal with those cases in detail. However, as the case of *Eli Lilly and Company (Canada) Limited v. The Minister of National Revenue* (1) was submitted to be indistinguishable from the case at bar I should point out that in that case the relationship between the appellant and its parent company was throughout that of vendor and purchaser and the account, on the payment of which the saving held to be taxable was made, was a merchandise account for goods sold and delivered.

For the reasons given by Mr. Fisher and for those set out above I would allow the appeal and restore the decision of the Income Tax Appeal Board with costs throughout.

Appeal dismissed with costs, CARTWRIGHT J. *dissenting.*

Solicitors for the appellant: Phillips, Bloomfield, Vineberg & Goodman, Montreal.

Solicitor for the respondent: A. A. McGrory, Ottawa.