1964
Oct. 8
Oct. 29

BETWEEN:

TALON EXPLORATION LTD. .. ..APPELLANT;

AND

THE MINISTER OF NATIONAL REVENUE } RESPONDENT.

Revenue—Income—Income tax—Acquisition and sale of carried interest in oil lands—Sale of potential income producing assets—Adventure or concern in the nature of trade—Income Tax Act, R.S.C. 1952, c. 148, ss. 3, 4 and 139(1)(e).

This is an appeal from the re-assessment of the income of the appellant for the taxation year 1957 wherein the respondent included therein a sum representing the appellant's profit resulting from its acquisition and sale of certain petroleum interests in Western Canada.

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The appellant was incorporated in July 1954 under the Alberta *Companies Act* and had as its objects to prospect, explore, drill, produce and accumulate petroleum, natural gas and related hydrocarbons and to open, drill, develop, improve, maintain and manage petroleum and natural gas wells and natural gas property generally. All the issued shares of the company were held by one Harris Cox and his wife and son, Harris Cox being its president and major shareholder. Before incorporating the appellant company Cox was employed for many years in seismographic work in connection with the discovery of oil, in Canada and other countries. The appellant entered into three agreements, each with a different oil company, and one agreement with the Province of Saskatchewan, the appellant agreeing in each case to drill for oil on the lands described in the agreements at its own expense, in return for which it was given an interest in the said lands. In each case the appellant arranged for other companies or individuals, including one Ross H. Chamberlain, with respect to all four drilling agreements, to finance the full cost of drilling in return for which the appellant's interest in the properties was transferred to them subject to a carried interest, usually of 15% being reserved to the appellant.

When Humber Oils Ltd. offered to buy Chamberlain's interests in the lands in question, the offer included the carried interests held by the appellant. The appellant's carried interests were sold to Humber Oils Ltd. along with Chamberlain's interests in the said lands.

The issue to be decided is whether the purchase or acquisition in 1954 of the carried interests of the appellant from Chamberlain and their sale in conjunction with the interests of Chamberlain in 1957, was an adventure or concern in the nature of trade so that the profit therefrom constituted taxable income, or whether what was done was the realization at an enhanced price of capital assets or investments and as a consequence did not constitute an adventure or concern in the nature of trade.

Held: That it is a fair inference from the evidence to conclude that Chamberlain wished to sell his interests to Humber Oils Ltd. and that while there may not have been too great reluctance on the part of the appellant to sell its carried interests, nevertheless, because of the history of the assistance given to the appellant by Chamberlain it would have been impractical and unrealistic for the appellant not to have concurred in the decision made by Chamberlain to sell.

2. That what Humber Oils Ltd. acquired was in effect a business as a going concern, and it acquired it by way of purchasing the investment interests of Chamberlain and the appellant in the properties affected by the first two drilling agreements executed by the appellant.

3. That the carried interests in question were acquired by the appellant as potential income-producing assets.

4. That the acquisition and sale of the carried interests of the appellant were transactions in capital assets and were not adventures or concerns in the nature of trade within the meaning of s. 139(1)(*e*) of the *Income Tax Act*.

5. That the appeal is allowed.

APPEAL from a decision of the Tax Appeal Board.

The appeal was heard by the Honourable Mr. Justice Gibson at Calgary.

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R. A. MacKimmie, Q.C. for appellant.

H. J. MacDonald, Q.C. and *T. E. Jackson* for respondent.

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

GIBSON J. now (October 29, 1964) delivered the following judgment:

This is an appeal from the judgment of the Tax Appeal Board which dismissed the appellant's appeal from a re-assessment made by the Minister for the 1957 taxation year wherein the Minister included in the appellant's income, *inter alia,* the sum of $58,685.69, which the Minister assessed as being profit constituting income arising out of the acquisition and sale by the appellant of certain petroleum interests in Western Canada.

The appellant company was incorporated in July, 1954. Under letters patent issued pursuant to provisions of *The Alberta Companies Act,* it had as its objects to prospect, explore, drill, produce and accumulate petroleum, natural gas and related hydrocarbons and to open, drill, develop, improve, maintain and manage petroleum and natural gas wells and natural gas property generally.

All the issued shares of this company belonged at all material times to Mr. Harris Cox, his wife and son. The issued capital stock originally had a value only of $4 and any money this company received initially to carry on its activities was supplied to it by way of loans from its president and major shareholder, Mr. Harris Cox.

Mr. Harris Cox said he caused this company to be incorporated with the intent to build up an independent oil company; and to do so it was necessary for him after this incorporation to acquire properties which had a probability of containing oil, and to cause these properties to be drilled for oil and to get the wells as drilled into production.

In order to accomplish this, he made various deals in respect to which he gave evidence.

According to the evidence the deals were made in the manner described because the oil industry in its discovery and development stages requires huge risks to be taken and requires huge amounts of capital to be expended to develop producing wells, and at the same time there are relatively small quantities of land available for such development. These facts caused oil companies, big and small,

to spread risks with other persons and/or companies so that in the business practically all oil wells are developed by more than one person or company, under contractual arrangements among themselves, which are varied, sometimes complicated and almost never uniform.

This is sometimes true in the case of proven lands but always true in the case of unproven lands.

In connection with the latter, the acquisition and drilling of unproven lands is sometimes referred to in the oil industry as "wild-catting".

According to the evidence the activities of certain individuals in obtaining leases in unproven lands has caused them to be called in the industry, in some cases, "lease hounds". Such persons, if they carried on this kind of activity in real estate transactions, would be looking for what are sometimes called "finder's fees".

It was stated that so-called "lease-hounds" do not participate in any way in the development of the property after obtaining leases, as for example in the way of drilling and otherwise developing the properties, but instead they receive only a fee for their services. The evidence also is that such persons seldom, if ever, receive any shares of any interests in the properties for their services, but instead, as stated, receive money for their services.

In making these deals concerning properties which potentially may contain oil or gas, it appears that the first thing that has to be provided for is a royalty to the land owner who is usually a farmer or the Crown. It is usually 12½% and is payable from the gross revenues obtained from the property whether or not the proceeds from the property result in a profit from operations or not.

Then, sometimes, in respect to a given property there is an interest called a "carried interest". In such a case the party owning the "carried interest" puts up no money for drilling costs or other expenses for the development of the mine. If such well or mine becomes profitable after it gets into production, then the costs that the other participating interests incurred for drilling and other charges are recouped first out of the revenues, and then after that the "carried interest" shares with the participating interests in the net profit according to the respective proportions of their ownership.

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At this stage the "carried interest" becomes a "working interest" and its owner becomes liable for the expenses subsequently incurred in the development and operation of the mine, but also, of course, entitles the owner of it to participate in the management proportionate to its relative share interest in the mine. In this way, the carried interest then becomes subject to what is called the "working agreement" which is the main agreement spelling out all the details of how the development and operation of the mine is to be done and what costs may be incurred and so forth.

Then there is sometimes what is called a "working interest" which is a full participating interest, which bears at all times its proportionate share of the expenses of development and operation of the mine.

There is also another interest which is carried and it is units in a royalty agreement. Royalty units usually belong to the owner of the minerals who is usually the farmer or the Crown.

The evidence indicated that any of the interests in mining properties outlined above may be earned in many ways, other than by putting up cash; and the largest of oil companies try to avoid putting up money or incurring drilling costs in unproven lands and often obtain interests in such lands without the expenditure of monies by them.

The result of all the activity by the appellant (which is detailed below) was that it did obtain some interests in unproven lands and that in the acquisition of these interests the appellant neither put up nor paid any money but instead earned them by providing certain technical services and "know-how".

The four transactions which resulted in the appellant obtaining petroleum interests were prescribed in certain agreements and documents which are filed in this appeal and are Exhibits 2 to 16.

The evidence of the president of the appellant, Mr. Harris Cox, however, was that the preparation and execution of each of these documents followed the actual events and that in certain respects these documents do not tell exactly what took place. However, the end result was that they

show that the appellant did receive interests in oil and gas properties out of these four transactions and the precise nature of these interests which it obtained is accurately described in these documents.

The situation was that prior to July, 1954, when Mr. Harris Cox caused the appellant company to be incorporated, he was employed in certain other endeavours. From 1931 until 1954, save and except for war service, he was employed by a company known as Geophysical Services Inc., of Dallas, Texas, which employment lasted until the war years, and after that he was employed by Western Geophysical Company. With the former company, he did seismograph work, which is a service rendered to oil companies who are interested in finding oil. This service is rendered complimentary to the services rendered by geologists; and as a result of putting together the information obtained from the rendering of such services, a recommendation is made to oil well clients advising them of the probable best places to drill for oil.

Mr. Cox performed his services with these two companies in the United States, in South America, the Indian Netherlands, and in Canada.

In 1954 Mr. Cox was employed by Western Geophysical Company in Canada, and at that time decided to leave that company to set up his own oil company, the appellant herein.

The first transaction that the appellant company entered into was with Canadian Superior Oil of California Ltd., and this took place in July of 1954. For the appellant, Mr. Harris Cox made a verbal agreement with that company to drill a minimum of ten wells on property which the latter held on lease, and in return the appellant received a 50% interest subject to the royalty in favor of the owner of the land. This verbal agreement was consumated after he had visited the properties with representatives of Canadian Superior Oil of California Ltd.

Mr. Cox then arranged with Dome Exploration Ltd. to put up 50% of the drilling costs, with Ross H. Chamberlain to put up 25% of these costs and with Welton Becket to

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put up 25% of these costs. In other words, he arranged with these three persons to take over and put up all the cash obligations in the drilling contract he had made with Canadian Superior Oil of California Ltd.

In the result, therefore, subject to a 12½% royalty to be paid to the owner of the land, there resulted the following percentage interests in this farm-out property from Superior Oil of California Ltd.:

50 % to Canadian Superior Oil of California Ltd.,
25 % to Dome Exploration Ltd.,
12½% to Ross H. Chamberlain, and
12½% to Welton Becket.

However, from the interests sold to Ross H. Chamberlain and Welton Becket, the appellant retained a 12½% "carried interest".

In the net result then the appellant ended up with a 3⅛% interest in the property which was a "carried interest". These arrangements are supported in evidence by Exhibits 2, 3, 4, 5, 6, 7 and 8 filed in this appeal.

The second transaction the appellant entered into was with Imperial Oil Ltd. in 1954 and it concerned the Midale field in Southern Alberta, and consisted of a quarter section or 160 acres.

Imperial Oil Ltd. held the lease from the farmer-owner in this unproven property and it was subject to a 12½% royalty to the owner.

Originally, Imperial Oil Ltd. in the negotiations with the appellant wanted a straight 10% royalty, which in the opinion of the appellant would have been most uneconomic for it and as a result there were further negotiations which ended in different arrangements being made.

The final arrangement made with Imperial Oil Ltd. required the appellant to drill the property and there was reserved to Imperial Oil Ltd. a 2½% royalty. This resulted in a 15% royalty payable, being 12½% to the farmer-owner and 2½% to Imperial Oil Ltd.

The appellant at the same time also obtained an option to drill on some Canadian Superior of California Ltd. property nearby, which in the event that the option was exercised by the appellant would give Canadian Superior Oil of California Ltd. a 2½% royalty.

The appellant then arranged with Dome Exploration Ltd. and the said Ross H. Chamberlain and Welton Becket to assume these costs of the drilling of these properties and also reserved to itself a 15% carried interest out of the interests sold to Chamberlain and Becket.

This resulted in the interests in these properties being as follows, namely, 50% to Dome Exploration Ltd., 25% to Ross H. Chamberlain, 25% to Welton Becket; and out of each of the interests of Chamberlain and Becket there was reserved to the appellant a 15% carried interest; so that in this transaction the appellant obtained a 7½% interest in the whole which was a carried interest.

The third transaction concerned property in the Province of Saskatchewan and was made in the fall of 1956 and was a reservation of land obtained by way of bid from the Province of Saskatchewan. This bid was made on a net royalty basis and in this bid the appellant joined with West Canadian Petroleum Ltd. and Westburne Oil Development Ltd. so that in the result each obtained a one-third interest in this reservation of land.

In this case the bid was such that an 87½% interest was to belong to the Crown once the property became a working property. In other words the Crown in this arrangement was to receive a 12½% gross royalty immediately on production, and then if and when the property became profitable, the Crown would receive 87½% of the net income.

The appellant in respect to this third transaction again went to Dome Exploration Ltd. and to Welton Becket who were not interested in buying into this one-third interest of the appellant, but Ross H. Chamberlain was interested and did assume the whole of the cash obligation of this one-third interest and reserved to the appellant a 25% carried interest therein.

The fourth transaction took place in December, 1956, and concerned property near the Virden Airport on which BA Oil Company Ltd. had a lease and in respect to which lands it was reluctant to develop by way of drilling because of danger to the airport facilities and adverse publicity if anything untoward should happen, and the appellant made a deal with it to drill which agreement was subject to a 50% carried interest in favor of BA Oil

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Company Ltd. In other words, the appellant assumed 100% of the drilling costs in this arrangement.

Then the appellant arranged with Ross H. Chamberlain to put up all the funds for this 100% of the drilling costs but reserved to the appellant a 25% carried interest.

The result was that this whole transaction was subject to a 50% carried interest in favour of BA Oil Company Ltd. and a 25% carried interest in favour of the appellant; and Ross Chamberlain had the other 25% which was the only full participating interest.

The evidence was that Mr. Cox for the appellant acquired all these interests in the four transactions and made deals with the other parties involved, namely, Dome Exploration Ltd., Ross H. Chamberlain and Welton Becket; that in these transactions Mr. Cox as president of the appellant company worked with Dome Exploration Ltd. which latter company was the operator company, in getting these properties drilled (and some of them into production as mentioned hereafter) and also successfully negotiated contributions from other persons or corporations who had leases in the various adjoining areas where such drilling was done, obtaining from them what is known as "dry hole money", being a contribution towards the drilling costs.

In all these efforts in working with Dome Exploration Ltd., thirty-three wells were drilled and fourteen of these were dry holes and nineteen were producers.

The appellant through its president Mr. Harris Cox was involved in the full program which caused these wells to be producers. In some cases the wells had his name joined in them, as, e.g., Harris Cox-Dome Well No. so-and-so.

The evidence was that the drilling costs for the cheapest well ran from $15,000 to $20,000 to a high for the most expensive of $75,000.

Subsequently, the interests in the transactions which were reservation lands from the Province of Saskatchewan the appellant disposed of in circumstances which are not relevant on this appeal, but in respect to the profit on the realization of which the appellant paid income tax.

The appellant subsequently did also sell the "carried interests" which he had received from Ross H. Chamberlain and the issue on this appeal is how the profit realized on

this sale should be categorized with reference to the provisions of the *Income Tax Act*.

The appellant still owns the carried interests which it obtained from Welton Becket.

The circumstances under which the carried interests which the appellant obtained from Ross H. Chamberlain were sold are briefly as follows: The brokerage and underwriting firm of Dougherty, Roadhouse & Co. of Toronto incorporated a company known as Humber Oils Ltd. and were anxious to acquire proven oil and gas properties for Humber Oils Ltd. in order to make it a producing company. It was necessary before the shares of this company could be listed on the Toronto Stock Exchange for it to own interests in proven properties. Mr. Darcy Dougherty approached Mr. Harris Cox to find out whether the Chamberlain interests were for sale and Mr. Cox referred him to Mr. Ross H. Chamberlain who at that time resided in San Francisco and was a broker and underwriter, and there subsequently was a meeting in San Francisco of all interested parties.

(Ross H. Chamberlain, as is patent from the summary of the evidence recorded above, had been a sort of financial "angel" of the appellant and had taken up and assumed, at all material times, a substantial part of the drilling cost obligations of the appellant in respect to all the transactions which are above recited. The appellant was dependent to a large extent on him for these costs; and had received for what it contributed to these transactions the carried interests above referred to.)

As a result, Humber Oils Ltd. (after the conference in San Francisco at which were present representatives of Dougherty, Roadhouse & Co. certain officers of the Humber Oils Ltd., Ross H. Chamberlain and certain of his associates, and officers of the appellant) purchased the Chamberlain interests in the first two transactions recited above, and also the carried interests of the appellant which the latter had received from the Chamberlain interests.

The purchase price was determined by negotiation after an appraisal had been made for Humber Oils Ltd. of the market value of these interests; and the offer made and accepted was substantially less than that suggested as the proper price in the so-called Sproule Valuation Report, which Chamberlain had obtained valuing these properties.

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The evidence was that the Sproule report did not separate on a valuation basis the interests of the appellant from the Chamberlain interests and the whole negotiations were carried on by Chamberlain on the basis that the carried interests of the appellant would be included in the sale.

It is a fair inference from the evidence to conclude that Ross H. Chamberlain wished to sell to Humber Oils Ltd. at this material time and he unquestionably was the dominant figure in the proposal and the arrangements to sell to Humber Oils Ltd.; and that while there may not have been too great reluctance on the part of the appellant to sell its carried interests, nevertheless, because of the history of the assistance given to the appellant by Chamberlain it would have been impractical and unrealistic for the appellant not to have concurred in the decision made by Chamberlain to sell.

It is relevant to observe also that what was sold were properties which were proven which is what Humber Oils Ltd. needed so that its underwriters could list its shares on the Toronto Stock Exchange and sell them to the public. Humber Oils Ltd. was not interested in buying nor did it buy unproven properties. In other words, what the Humber Oils Ltd. did acquire was in effect a business as a going concern; and it acquired it by way of purchasing the investment interests of Chamberlain and the appellant in the two properties referred to in the first two transactions recited above.

This conclusion is arrived at by considering the whole of the evidence given by Mr. Louis Diehl, secretary-treasurer of Hitchcock and Chamberlain Ltd. (of which Ross H. Chamberlain was the major owner), and who was familiar with the sales transaction with Humber Oils Ltd., Dr. E. D. Alcock who acted as a geologist advisor and who had very considerable experience in the oil industry and who appraised for Humber Oils Ltd. the interests of Chamberlain and the appellant in these producing wells and who also gave evidence that Humber Oils Ltd. tried to buy the Becket interest in these properties but was unsuccessful, and also the evidence of the appellant.

Counsel for the appellant submitted that these transactions resulted in a capital gain and the transactions should not be considered solely from the intention of the party but their characterization should also be determined from what

the appellant actually did; and in this particular case what the appellant actually did was more important.

Counsel submitted that Cox, president of the appellant, was a trained engineer in the oil industry; that he left his employment and formed a small company, the appellant, whose objects are set out in the memorandum of association filed as Exhibit 1, referred to above; that the appellant showed what it did in acquiring these interests and demonstrated that it obtained these carried interests for the purpose of obtaining future income from producing wells, which corresponded with its declared intention and that in this business, the high cost of drilling was so important that even though the appellant did not have money to drill the evidence was that this was not a great criteria, because oil companies, big or small, always tried to get someone else to incur the drilling costs in "wild-cat" drilling in unproven areas; that the appellant made these deals with Canadian Superior Oils Co. of California and Imperial Oil Ltd. and the subsequent deals with Dome Exploration Ltd. and Chamberlain and Becket, and from the two latter he got these small carried interests; that Chamberlain was the financial "angel" of the appellant during this period; and that what the appellant got was nothing like a "finder's fee" but instead were interests in future income and these interests became valuable because the appellant worked to get the mines into operation; that when Mr. Dougherty of Dougherty, Roadhouse & Co. contacted the president of the appellant, he immediately referred him to Ross H. Chamberlain, and although Mr. Cox attended the negotiating meetings in San Francisco "the situation was delicate" (as Mr. Cox put it) and that Mr. Cox thought that Chamberlain wanted to sell, and the appellant really had no practical alternative but to sell.

From this evidence the appellant submits that it was reasonable for it to sell when Chamberlain saw the opportunity and wished to sell because the appellant did not want to frustrate Chamberlain's effort especially in view of his history as a financial backer, and as a consequence the appellant did sell its interests, but this did not make the appellant a trader in securities. Up to that time it had been a developer of these properties, working closely with Dome Exploration Ltd., the operator, and that this transaction in which the appellant concurred in Chamberlain's resolution

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to sell, under the circumstances, did not change the appellant from being a small operator of mines doing reasonably well into a trader in security interests in such mines.

In this latter connection, Mr. Cox for the appellant stated that the appellant is currently receiving a small income of about $300 a month from the "carried interests" obtained through the Becket interests in these properties.

Counsel for the appellant also stated that in effect the appellant exchanged one form of investment for another in this transaction, that is, it exchanged the carried interests for shares in Humber Oils Ltd. and some cash, and on the evidence, its intent and conduct go together to substantiate that it was not a trader of securities.

Counsel for the respondent to the contrary argued that the profit from the transactions was income within the meaning of section 3 of the *Income Tax Act;* that the property was not being taxed, but it was the taxpayer who was being taxed; that in a given case the receipt of an asset exchanged can be capital in one company and income in the other company with whom the former dealt; that there was only one business that Talon was engaged in and that was to make money; that the only time the appellant made any money was when it sold assets it had acquired; that the only thing the appellant had to offer at any material time was the knowledge, experience and the contribution that its president could make; that what it did was put several deals together as a promoter and therefore a dealer; that this was the business of the company, namely, putting transactions together; that with respect to the contract which is the subject of this appeal, the appellant negotiated with Canadian Superior Oils of California and with Imperial Oils Ltd. and then went to Dome Exploration Ltd. and Chamberlain and Becket and that it did not matter whether the interest received by the appellant came only from Becket or Chamberlain, the important thing was that it received an asset in the production of these properties; that what the appellant got for its services and contributions was an interest in the production of the wells and it was that interest that the appellant sold and converted into cash; that any company in order to make a profit must receive cash; and the only way that the appellant could get cash was to sell what it had acquired and it did not matter what method

was followed if that was the business of the company, as was the case here.

On these facts and submissions I am of the opinion following:

In the consideration of this matter, the applicable sections of the *Income Tax Act*, R. S. C. 1952, c. 148, in the determination of this appeal are sections 3, 4 and 139(1)(*e*) which read as follows:

3. The income of a taxpayer for a taxation year for the purposes of this Part is his income for the year from all sources inside or outside Canada, and, without restricting the generality of the foregoing, includes income for the year from all

(*a*) businesses,

(*b*) property, and

(*c*) offices and employments.

4. Subject to the other provisions of this Part, income for a taxation year from a business or property is the profit therefrom for the year.

139.(1) In this Act

. . .

(*e*) "business" includes a profession, calling, trade, manufacture or undertaking of any kind whatsoever and includes an adventure or concern in the nature of trade but does not include an office or employment;

The issue to be decided here is whether the purchase or acquisition in 1954 of the carried interests of the appellant from Ross H. Chamberlain and their sales in conjunction with the interests of Ross H. Chamberlain, in 1957, was an adventure or concern in the nature of trade so that the profit therefrom constituted taxable income, or whether what was done was the realization at an enhanced price of capital assets or investments and as a consequence did not constitute an adventure or concern in the nature of trade.

The respondent in his Reply to the notice of appeal sets out the issue in this way (pleading that in re-assessing he acted on the following assumptions) paragraph 15:

15. In re-assessing the Appellant for its 1957 taxation year, notice of which was posted on the 15th day of April, 1959, wherein he included in the Appellant's income, inter alia, the sum of $58,685 69, the Respondent acted on the following assumptions, inter alia:

(a) that in the course of its business the Appellant acquired interests in certain petroleum and natural gas properties in Canada, or in the proceeds of production therefrom;

(b) that the acquisition of interests in petroleum or natural gas properties or in the proceeds of production therefrom and the turning to account thereof at a profit constituted a business of the Appellant;

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(c) that in the course of the Appellant's business, the Appellant, in the taxation year 1957, disposed of the following interests at a profit of $58,685 69:

(i) 15% of the 25% interest acquired by one Ross H. Chamberlain in a farmout agreement dated July 2nd, 1954, made between Superior Oil of California Ltd. and Dome Exploration (Western) Limited;

(ii) 15% of the interest acquired by the said Ross H. Chamberlain in a farmout agreement dated October 21st, 1954, made between Imperial Oil Limited and Dome Exploration Limited;

(iii) 15% of the interest acquired by the said Ross H. Chamberlain in a farmout agreement dated November 1st, 1954, made between Canadian Superior Oil of California Ltd. and Dome Exploration (Western) Limited;

(iv) a 25% interest in the share of the said Ross H. Chamberlain in the gross proceeds of the production from certain properties in which the Appellant had had, together with West Canadian Petroleums Ltd. and Westburne Oil Development Ltd., a beneficial interest, which interest the Appellant had assigned to the said Ross H. Chamberlain by agreement dated July 1st, 1956;

(v) a 12½% interest in the petroleum substances produced from wells drilled on certain leased property in which the Appellant had assigned its interest to the said Ross H. Chamberlain by agreement dated September 14th, 1956.

(d) that the said profit constituted income from the Appellant's business for the 1957 taxation year.

In respect to this pleading, as Cattanach J. said in *Minister of National Revenue v. Pillsbury*[1].

> The respondent could have met the Minister's pleadings that, in assessing the . . . (appellant), he assumed the facts set out in paragraph . . . (15) . . . of the Notice of Appeal by:
>
> (*a*) challenging the Minister's allegation that he did assume those facts,
>
> (*b*) assuming the onus of showing that one or more of the assumptions was wrong, or
>
> (c) contending that, even if the assumptions were justified, they do not of themselves support the assessment.

The appellant on this appeal adopted the course outlined in (b) above.

As a result from the evidence adduced the question to be decided might be put in several ways, as for example: Was the appellant in the business of trading in securities when it acquired and disposed of these carried interests? Did these transactions constitute dealing in mining securities? Is the proper inference to be drawn from these

[1] (64. D T C. 5184)

transactions that the appellant was not a developer but instead a trader?

As a guide in matters such as this, certain tests were laid down by the learned former President of this Court in the case of *Minister of National Revenue v. Taylor*[1]. At page 214 of the Canadian Tax Cases Report, Thorson P., after prescribing these certain guides, stated:

> . . . that the question whether a particular transaction is an adventure in the nature of trade depends on its character and surrounding circumstances and no single criterion can be formulated.

And in *Edwards v. Bairstow*[2], Lord Radcliffe stated at page 38:

> Dealing is, I think, essentially a trading adventure, and the respondents' operations were nothing but a deal or deals in plant or machinery.

In this case in brief, therefore, was this then a deal or deals in purchasing mining securities?

Or was the transaction simply this—Was the acquisition of these carried interests by the appellant at the material times made for the purpose of obtaining revenue and therefore in the nature of capital investment within the meaning of the *Irrigation Industries Ltd. v. Minister of National Revenue*[3] and *Montreal Trust Company v. Minister of National Revenue*[4] cases and was the gain or profit on the realization of such capital assets or investments capital?

The evidence adduced by the appellant in my opinion proves that in substance the assumptions of the Minister contained in paragraph 15 of the Reply in the pleadings are wrong.

The evidence established that these carried interests were acquired by the appellant as potential income producing assets; that the appellant with Dome Exploration Ltd. had developed the properties, in which there were these carried interests, so that nineteen wells were brought into production; that Humber Oils Ltd., the purchaser of these carried interests was only interested at the material time in buying proven properties, i.e., income producing properties; and that Chamberlain was the dominant person who made the effective decision to sell to Humber Oils Ltd.; and that in the circumstances it would have been

[1] [1956] C.T.C. 189. [2] [1956] A.C. 14.
[3] [1962] S.C.R. 346. [4] [1962] S.C.R. 570.

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impractical and unrealistic for the appellant not to have gone along with or concurred in Chamberlain's decision to sell.

In my opinion, therefore, the evidence proves that the acquisitions and sales of these carried interests of the appellant were transactions in capital assets, and neither were an adventure or concern in the nature of trade within the meaning of section 139(1)(*e*) of the *Income Tax Act* and therefore any profit or gain is not income within the meaning of section 3 of the Act.

The appeal is therefore allowed with costs.

Judgment accordingly.