1957
Feb. 22
Sept. 11

ARRCO PLAYING CARD COMPANY (CANADA) LIMITED } APPELLANT;

AND

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

Revenue—Income tax—Deductions—Legal fees paid to secure reduction on import duties—Whether disbursement for purpose of gaining income or payment on account of capital—The Income Tax Act, S. of C. 1948, c. 52, s. 12(1)(a) and (b)—Customs Tariff, R.S.C. 1927, c. 44 as amended, s. 1 and Schedule A, Part III, items 194, 194(a).

The appellant, a manufacturer of playing cards, imported lithographed sheets used in their manufacture which under item 194 of the *Customs Tariff*, R.S.C. 1927, c. 44, as amended (now R.S.C. 1952, c. 60), were subject to an equal amount of duty as that charged on manufactured playing cards. The appellant believed the duty imposed unfair and retained a lawyer to submit its views to the taxing authorities. As a result of the latter's representations, the Act was amended and item 194(*a*) added, resulting in a substantial reduction on the duty on lithographed sheets when imported by manufacturers for the manufacture of playing cards in their own factories. The sum paid the lawyer, deducted by the appellant from its taxable income, was disallowed by the Minister on the grounds that the outlay was not incurred for the purpose of gaining income from the appellant's business within the meaning of s. 12(1)(*a*) but was a payment on account of capital under s. 12(1)(*b*) of the *Income Tax Act*.

Held: That the purpose of the expenditure was to secure by means of a modification of the tariff a long term advantage and such expenditure constituted a payment on account of capital, the deduction of which is prohibited by s. 12(1)(*b*) of the *Income Tax Act*. *Minister of National Revenue v. Dominion Natural Gas Co. Ltd.* [1941] S.C.R. 19; *Montreal Light, Heat & Power Consolidated v. Minister of National Revenue* [1942] S.C.R. 89; *Minister of National Revenue v. Siscoe Gold Mines Ltd.* [1945] Ex. C.R. 257 at 261; *Thompson Construction (Chemong) Ltd. v. Minister of National Revenue* [1957] Ex. C.R. 96 at 102, followed. *Minister of National Revenue v. Kellogg Co. of Canada Ltd.* [1943] S.C.R. 58; *Minister of National Revenue v. L. D. Caulk Co. of Canada Ltd.* [1954] S.C.R. 55, distinguished.

APPEAL from a decision of the Income Tax Appeal Board. (1).

The appeal was heard by the Honourable Mr. Justice Kearney at Montreal.

Leon Crestohl, Q. C. and *Lazarus Tinkoff* for appellant.

K. E. Eaton and *W. R. Latimer* for respondent.

(1) 12 Tax A.B.C. 230; (1955) 55 D.T.C. 135.

KEARNEY J.:—This is an appeal from a decision of the Income Tax Appeal Board (1), dated February 4, 1955, dismissing an appeal by the taxpayer from a re-assessment applicable to its taxation for the year ending June 30, 1951.

The appellant deducted from its 1950-51 income some $11,000, representing fees and disbursements paid during the said year to its attorney for professional services rendered in procuring favourable modifications in the *Customs Tariff* affecting materials imported by the appellant from the United States.

The deduction was disallowed because, according to the respondent, the outlays in question were not incurred by the taxpayer for the purpose of gaining or producing income, within the meaning of s. 12(1)(*a*) of *The Income Tax Act,* S. of C. 1948, c. 52, but were outlays on account of capital, within the meaning of s. 12(1)(*b*) thereof.

Counsel for the appellant submitted that s. 12(1)(*b*) has no application as the expenditure was in no sense an outlay on account of capital, but clearly one made for the purpose envisaged in the exceptive provision contained in s. 12 (1)(*a*).

Section 12 reads in part as follows:

> 12. (1) In computing income no deduction shall be made in respect of
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from property or a business of the taxpayer,
> (*b*) an outlay, loss or replacement of capital, a payment on account of capital or an allowance in respect of depreciation, obsolescence or depletion except as expressly permitted by this Part.

The appellant company was incorporated in December 1949 and began operations in July 1950, with the result that its first fiscal year ended June 30, 1951. At some time it imported playing cards from the United States in finished form, but during its first year of operations it engaged in the business of manufacturing playing cards in Toronto and found it necessary to import cards in the form of lithographed sheets from the United States. Twenty-seven cards were lithographed on each sheet and two such sheets formed a unit which represented about 35 per cent of the manufactured cost of a finished deck. Manufacture of the sheets into complete ready-for-sale

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decks was carried out in the appellant's plant by processes known as punch pressing, sanding, gilting, deck and box wrapping.

The appellant found that the rate of duty applicable was seven cents per deck, whether imported in a complete state of manufacture or in the form of sheets which required the aforesaid finishing processes. Moreover, the duty of seven cents per deck applied, whether the material was of a quality to constitute a high or a low-priced deck.

The appellant considered the existing import duty contained in item 194 of the *Customs Tariff* unfair and authorized its attorney to obtain, if possible, a rectification thereof and a reduction in the existing duty of seven cents per unit. The appellant's attorney succeeded in having a new item, 194a, added to the *Customs Tariff*, which fixed a duty of 20 per cent of the value of the imported unit in the form of sheets. As a result the appellant paid in the fiscal year 1950-51 $29,734 less in customs duties, and on future imports will continue to derive a similar advantage so long as the existing legislation remains in force. Omitting the rate of duty applicable, the two aforesaid tariff items read as follows:

194. Playing cards, in packs or in sheet form, n.o.p.; cards and sheets partly lithographed or printed, for use in the manufacture of such playing cards . . ."

194*a*. Wholly or partially lithographed or printed sheets when imported by manufacturers of playing cards for use exclusively in the manufacture of playing cards in their own factories.

Item 194, as set out above, resulted from an amendment in 1937 (S. of C. 1937, c. 26, s. 2) to *An Act Respecting the Duties of Customs*, or to give it its short title, the *Customs Tariff* (R.S.C. 1927, c. 44 now R.S.C. 1952, c. 60). Owing to parliamentary delays, item 194*a* was not enacted until 1952 (S. of C. 1952, c. 23, s. 1 and Schedule A, Part III), but in the meantime the appellant received the benefits contained in the said item by means of two Orders-in-Council, P.C. 5744 dated November 29, 1950 (Ex. 3) and P.C. 4611 dated September 5, 1951 (Ex. 4). Furthermore, P.C. 5744 was made retroactive to August 1, 1950, and the appellant received a refund of some $13,000, which was included in the amount of $29,734 previously mentioned.

Counsel for the respondent submitted that, first and foremost, the purpose and effect of the services for which appellant's attorney was paid were to secure an enduring benefit in the form of a continuing tariff advantage for the appellant and that, therefore, the cost of those services was a payment on account of capital, the deduction of which is prohibited by s. 12(1)(*b*).

Alternatively, it was submitted that the cost of the said services was an outlay or expense not made or incurred by the appellant for the purpose of gaining or producing income from the appellant's business and therefore its deduction was prohibited by s. 12(1)(*a*).

In support of the alternative statement, it was also submitted that, because the expenditure was made to decrease cost or save expense, it could not be said to have been made for the purpose of gaining or producing income, or to have been directly related to that purpose. Likewise, since it was made to secure from the government a concession in customs duties or taxes, it could not have been made for the purpose of gaining or producing income *from the business* of the appellant. In addition, it was not directly related to the earning of income notwithstanding that incidentally it had the effect of increasing income.

Counsel for the appellant supported his submissions by the following statements. Not only the purpose but the effect of the expenditure was to produce income. The advantage received must be regarded not as an enduring but as a short term benefit. The benefit was not an exclusive one and the appellant had no assurance that it would not be withdrawn. Moreover, even admitting that the expenditure had been made to secure an enduring benefit, it nevertheless should not be regarded as a payment on account of capital as its deduction is permissible under ordinary principles of commercial trading and accepted business practice; and under these same principles it could not properly be set up on the company's books of account as a capital asset and depreciated.

I think it is of first importance to determine if the $11,000 paid to the attorney constituted a payment on account of capital, within the meaning of s. 12(1)(*b*) because, as pointed out by counsel for the respondent, provided the deduction were found to be prohibited by para.

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(*b*), further enquiry into whether it fell outside or within the exceptive provision of para. (*a*) could be dispensed with. On the other hand, such enquiry would be necessary in the event of a finding that the deduction was not excluded by para. (*b*). Authority for this statement is found in the observations of Thorson P. in *Siscoe Gold Mines Ltd. v. Minister of National Revenue* (1) when dealing with the corresponding paragraphs (*a*) and (*b*) of s. 6 of the *Income War Tax Act*. The same reasoning was recently applied to s. 12(1)(*a*) and (*b*) of the *Income Tax Act* by Cameron J. in *Thompson Construction (Chemong) Ltd. v. Minister of National Revenue* (2).

In determining whether or not the deduction was excluded by para. (*b*), I will begin by considering the purpose of the expenditure and the nature of the benefit sought. The General Manager testified (pp. 7 and 12 of the transcript) that the sole purpose of the expenditure was to reduce the duty from seven cents per deck in sheet form to twenty per cent of the value thereof, which made a difference of four cents per pack.

The evidence of the attorney shows that the services performed by him were related to securing a rectification in the tariff, which he considered could not be brought about otherwise than by a statutory amendment, (p. 26 of the transcript). It shows also that, because "the House was not in session," delays occurred in securing the statutory amendment, and it was only as an interim measure that the attorney asked to have an Order-in-Council passed (p. 23). This was done and in fact a second one was required. Even the first Order-in-Council had to be delayed pending the result of an International Tariff Conference in England which the attorney attended (p. 21). Only because of this was it made retroactive and did the appellant receive a refund of some $13,000. Although the General Manager of the appellant made some reference to a rebate, I do not think he contended that it was sought, and the following evidence of the attorney, at p. 24, plainly shows that such was not the case.

> The Tariff Commissioner drew to my attention that to right this wrong he would even recommend that the Order-in-Council be made retroactive, which produced for the company an additional $13,000 profit

(1) [1945] Ex. C.R. 257 at 261. (2) [1957] Ex. C.R. 96 at 102.

for that one year, and we recovered a cheque for some $13,000. I did not even go to seek that, but as a result of my efforts that was a by-product, and to the company a very healthy and desirable by-product.

Thus the evidence does not support the suggestion that the appellant's purpose was to secure a refund or a benefit limited to the duration of an Order-in-Council.

Again, at p. 14, the same witness, speaking of the extent and duration of the benefit, said:

A. If the tariff does not change we actually gain as long as the tariff remains as it is.

Q. And you might expect to get $29,000 each year?

A. Depending on business conditions.

Q. Has the tariff been changed since?

A. The tariff has not been changed, no.

In the light of the foregoing evidence, and also because it was so much in the interest of the appellant to secure a favourable modification in the tariff for as long a period as statutory rights would give it, I find that such was the appellant's purpose.

It is true, of course, that the amendment made to the *Customs Tariff* is not reserved for the sole use of the appellant. Nevertheless it is less general than item 194 and is applicable only to wholly or partially lithographed units "when imported by manufacturers of playing cards for use exclusively *in their own factories.*" This provision was made to fit the appellant's situation at its request and, although someone else who could conform to its requirements might avail himself of it, it still constitutes, in my opinion, and will likely continue to constitute an important benefit or advantage to the appellant.

It is likewise true, as argued by counsel for the appellant, that the company had no assurance that, once the amending Act was passed by Parliament, it would not at some later date be revoked or modified. For example, a change of policy at governmental level on tariff matters could result in a general increase or reduction in customs duties. However, in virtue of R.S.C. 1952, c. 158, s. 8, every federal statute is subject to amendment, alteration or repeal, by a subsequent Act, even if passed at the same session of Parliament during which the original Act was passed. This leads to the legal question of the duration of a statute.

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As pointed out at p. 61 in *Craies on Statute Law,* 5th Ed., Acts are classified by reference to their duration as temporary or perpetual.

(*a*) *Temporary.* Temporary statutes are those on the duration of which some limit is put by Parliament.

(*b*) *Perpetual.* Perpetual Acts are those upon whose continuance no limitation of time is expressly named or necessarily to be understood. They are not perpetual in the sense of being irrevocable.

And again under the title of "Duration of Statutes," at p. 374:

3. *Duration presumably perpetual.* Every statute for which no time is limited is called a perpetual Act, and continues in force until it is repealed.

The same statement appears in *Halsbury's Laws of England,* 2nd Ed.; Vol. 31, Art. 664, "The duration of a statute is *prima facie* perpetual."

In speaking of burden of proof, *Phipson on Evidence,* 9th Ed., p. 35, says:

(1) Where a disputable presumption of law exists, or a *prima facie* case has been proved, in favour of a party, it lies upon his adversary to rebut it.

I am of the opinion that in the present instance at least a *prima facie* case has been established and that we are dealing not with a temporary statute but with one which must be deemed to be perpetual.

There remains the important question of whether the expenditure should be attributed to capital or to revenue.

The appellant caused to be heard two chartered accountants. One of them, Mr. Parkinson, C. A., after saying he considered the expenditure deductible by the ordinary principles of commercial and trading practice and that, as an auditor, he thought he would oppose setting it up as an asset, made the following statement, p. 31 of the transcript, (which I think, in a measure recognizes the continuing nature of the benefit obtained): ". . . certainly we can use hindsight when we know the tariffs have not since been changed. Using hindsight we possibly could have amortized the cost of that charge over future years. On the other hand, trying to use foresight at the beginning where there is no guarantee that the benefit is to last indefinitely, and having regard to the fact that his (its) income was increased $29,000 in the year under review, it would be prudent business practice to deduct it completely."

Counsel for the respondent did not take issue with the concluding words of the opinion above expressed. He submitted that such complete deduction has been held to be prohibited for income tax purposes because the expenditure is regarded as an outlay to secure an enduring benefit, and that such decision must prevail over business practice or good accountancy. He then referred to *Minister of National Revenue v. Dominion Natural Gas Co. Ltd.* (1).

The legal expenses incurred in the case cited resulted from the defence of an action brought against the taxpayer by way of an attack on its franchise rights to continue to supply natural gas to parts of the City of Hamilton by a company which also claimed franchise rights therein. Duff, C. J., while stating that "in the ordinary course, . . ., legal expenses are simply current expenditure and deductible as such; but that is not necessarily so . . .," came to the conclusion that the expenditure should be attributed to capital. *Vide* p. 24.

> It satisfies, I think, the criterion laid down by Lord Cave in *British Insulated v. Atherton* (2). The expenditure was incurred "once and for all" and it was incurred for the purpose and with the effect of procuring for the company "the advantage of an enduring benefit." The settlement of the issue raised by the proceedings attacking the rights of the respondents with the object of excluding them from carrying on their undertakings within the limits of the City of Hamilton was, I think, an enduring benefit within the sense of Lord Cave's language . . .
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> * * *
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> The character of the expenditure is for our present purposes, I think, analogous to that of the expenditure in question in *Moore v. Hare* (3), where promotion expenses incurred by coalmasters in connection with two parliamentary bills giving authority to construct a line to serve the coalfield were held to be capital expenditures.

In the case of *Montreal Light, Heat and Power Consolidated v. Minister of National Revenue* (4), wherein the company sought to deduct as a current expense the expenditure made to reduce carrying charges on its bonds, Duff, C. J., at p. 92, again invoked what was said in the *Atherton* case in these terms:

> I think, moreover, that these disbursements were made for a purpose which falls within the principle enunciated by Lord Cave in the *British Insulated and Helsby Cables Ltd. v. Atherton* (5); that is to say, the expenditures were made with a view to securing an enduring benefit, the reduction of the cost of borrowed capital over a period of at least fifteen years.

(1) [1941] S.C.R. 19.
(2) [1926] A.C. 205 at 213.
(3) [1935] A.C. 431 at 440.
(4) [1942] S.C.R. 89.
(5) [1926] A.C. 205 at 212.

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When later heard before the Privy Council (1), the ensuing judgment was based not on the prohibition contained in s. 6(1)(*b*) of the *Income War Tax Act* but on that contained in s. 6(1)(*a*) thereof. Nevertheless Lord Macmillan, at p. 135, stated:

> . . . their Lordships in no way dissent from the view that the second objection (namely, that the expense was a capital one) also applies.

In argument, counsel for the appellant observed that instances are not lacking where legal expenditures have been attributed to revenue rather than to capital and, as no two cases are identical, each must be judged on its own merits. He particularly relied on *Minister of National Revenue v. L. D. Caulk Co. of Canada Ltd.* (2); *Minister of National Revenue v. Kellogg Co. of Canada Ltd.* (3).

In the *Caulk* case which distinguished the *Dominion Natural Gas* case, it was held that expenses incurred by the taxpayer in successfully defending itself against a criminal charge instigated by the government under the *Combines Investigation Act,* and in making representations to the Commissioner administering the said Act, were wholly, exclusively and necessarily laid out for the purpose of earning income. I do not think the principles applied in that case, wherein a branch of the government sought to prevent the taxpayer from carrying on business in its accustomed manner, are applicable in the instant case. Here the appellant is free to import its basic material without interference but seeks a new particular concession by way of diminished duties; and the immediate problem is to determine whether or not the appellant is deemed to have made a capital expenditure because the expenditure was made in order to obtain a continuing benefit or advantage. I do not think that such an issue arose in the *Caulk* case.

The same, in my opinion, is true of the judgment delivered by Duff, C. J., in the *Kellogg* case wherein the appellant had no reasonable alternative but to defend itself against injunction proceedings aimed at preventing it from making use of ordinary descriptive words in connection with the sale of its products. Here the appellant is not faced with the necessity of defending itself against

(1) [1944] A.C. 126. (2) [1954] S.C.R. 55.
(3) [1943] S.C.R. 58.

someone seeking to deprive it of its common law rights, but rather does it seek the enactment of a statute which will procure for it a long term advantage which it did not previously possess.

Although, admittedly, the facts in the *Dominion Natural Gas* and the *Montreal Light, Heat and Power* cases differ from those in the present one, I nevertheless feel bound to follow them because they contain certain criteria which, I believe, *mutatis mutandis*, are apposite herein.

The expenditure under consideration was, in my opinion, made once and for all to secure a benefit or advantage that was expected to be enjoyed over a lengthy though indefinite future period. The purpose which motivated the expenditure was the appellant's desire to pay less customs duties in the future than in the past. The fact that, in the last analysis, an increase in income should accrue to the appellant does not, I consider, affect the validity of the above-mentioned conclusion.

I therefore find that the expenditure in question should be regarded as constituting a payment on account of capital, the deduction of which is prohibited under s. 12(1)(*b*).

Since I find that the deduction sought is so prohibited, I do not think it necessary to discuss the respondent's alternative submission or the reasons advanced by the appellant in support of its contention that the case falls within the exceptive provision of s. 12(1)(*a*).

For the above-mentioned reasons, I consider that the appeal in this case should be dismissed with costs.

Judgment accordingly.