Montreal 1968
Oct. 8-9

BETWEEN:

CANADA STARCH COMPANY LIMITED ..... APPELLANT;

AND

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

Income tax—Deductions—Business income—Computation of—Lump sum paid to remove opposition to registration of trade mark—Whether payment on account of capital—Income Tax Act, s. 12(1)(b).

Appellant, which manufactured a cooking oil made from corn oil, decided in 1963 to place on the market a less expensive cooking oil made from soya bean oil in order to meet competition. With this in mind it employed advertising agents to suggest a name for the product, designers to design containers and labels, and a market survey firm to conduct a market survey. The name "Viva" was recommended for the new product but appellant's application for registration of that name as a trade mark was opposed by a grocery company which had registered the word as a trade mark. Following negotiations the grocery company abandoned its opposition on payment of $15,000, and appellant's application was duly granted.

Held, the $15,000 so paid by appellant, like the fees paid to the trade mark lawyers and the Trade Marks office, was a payment incidental to its ordinary trading operations, and therefore deductible in computing its income for the year; it was not a payment on account of capital and thus barred from deduction by s. 12(1)(*b*) of the *Income Tax Act*. Registration of a trade mark is of no value if the trade mark does not become distinctive in the course of the current operations of the business, and hence if the trade mark "Viva" was of enduring benefit to appellant's business it was not because of the $15,000 paid the grocery company.

M.N.R. v. Algoma Central Ry. [1968] S.C.R. 447; [1968] C.T.C. 161; *Sun Newspapers Ltd. et al v. Fed. Com'r. of Taxation* (1938) 61 C.L.R. 337, referred to.

INCOME TAX APPEAL.

Bruce Verchere for appellant.

M. J. Bonner for respondent.

JACKETT P. (orally):—This is an appeal from the appellant's income tax assessment for the 1964 taxation year in which the only question that I have to decide is whether a payment of $15,000 made by the appellant in that year to a third person in certain circumstances is deductible in computing its income for the year, or whether the

deduction of that amount is prohibited by section 12(1)(*b*) of the *Income Tax Act*, which reads as follows:

> 12. (1) In computing income, no deduction shall be made in respect of
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> * * *
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> (*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,
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> * * *

The circumstances in which the payment of $15,000 was made are set out in an "Agreed Statement of Facts", which reads in part as follows:

> 1. The Appellant's principal business is corn grinding from which the Appellant produces, *inter alia*, industrial starches and corn sweeteners for sale to manufacturers. In addition, the Appellant manufactures for sale by retailers, cooking oils known as "Mazola" and "VIVA" and other food products. Prior to 1963 the only cooking oil sold by the Appellant was "Mazola".
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> 2. Proctor & Gamble Company of Canada Limited was not, prior to 1964, a competitor of the Appellant in respect of the manufacture and sale in Canada of liquid cooking oil, but was a competitor of the Appellant in the sense that prior to 1964 Proctor & Gamble Company of Canada Limited sold in Canada a solid vegetable shortening under the trade name "Crisco".
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> 3. In the spring of 1963 the Appellant discovered that Proctor & Gamble Company of Canada Limited planned to market in Canada a liquid cooking oil under the trade name "Crisco". Such oil is less expensive to the consumer than the Appellant's oil, "Mazola", because "Crisco" is made from soya bean oil, which is less expensive than the corn oil used to produce "Mazola". Proctor & Gamble Company of Canada Limited did, in 1964, commence to sell "Crisco" cooking oil in Canada and has continued to do so to the present time.
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> 4. In the spring of 1963 the Appellant's marketing division recommended that a soya bean oil, comparable in price to "Crisco" (and therefore less expensive than "Mazola") be introduced and sold by the Appellant in Canada. The Appellant would thus be in a position to compete with the expected entry into the Canadian market of Proctor & Gamble Company of Canada Limited's liquid cooking oil, "Crisco". It was the opinion of the Appellant's marketing division that there was a substantial commercial advantage to be gained from the marketing of a variety of cooking oils rather than only the one brand, "Mazola".
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> 5. In or about April 1963, on the advice of the Appellant's Marketing Research Division, the Appellant's executive officers decided to test market a second and less expensive brand of cooking oil.
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> 6. In or about April 1963 the Appellant engaged the services of Baker Advertising Agency to suggest a product name for the proposed new cooking oil. . . . In or about May 1963 the Appellant's officers tentatively selected "VIVA" as the product name for the proposed new cooking oil.

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7. In June of 1963 the Appellant instructed Messrs. Herridge, Tolmie, Gray, Coyne & Blair, solicitors, of Ottawa, to advise it whether the word "VIVA" was available as a trade mark. The Appellant received a letter dated July 22nd, 1963, from the solicitors reporting upon the availability of the trade mark "VIVA". . . .

8. In June of 1963 the Appellant retained the services of Stewart & Morrison Limited, industrial designers, to design containers and labels for the Appellant's proposed new cooking oil, "VIVA".

9. In June 1963 the Appellant instructed Admetrics Limited to carry out a demographic survey of the cooking oil market as far as size, regional use and brand desirability were concerned.

10. During June of 1963 the Appellant expended the sum of $3,832.00 in respect of the Admetrics survey and the services performed by Stewart & Morrison Limited in preparing rough designs of a bottle and label for its proposed new cooking oil, "VIVA".

11. In or about June 1963 the Appellant adopted the code name "Brand X" for its new cooking oil "VIVA" in order to preserve as much secrecy as possible.

12. On July 8th, 1963, Messrs. Gowling, MacTavish, Osborne & Henderson, solicitors, of Ottawa, on Appellant's instructions, filed with the Registrar of Trade Marks an application for the registration of the trade mark "VIVA" for use in association with edible vegetable oils. . . .

13. In July of 1963 the Appellant engaged Louis Cheskin Associates, a firm carrying on the business of market research, to conduct a name association study to gauge the public response to the name "VIVA", and also to the names "Harvest", "Argo", "Senora" and "Puritan". The Appellant's marketing officials wished to investigate the acceptability of the proposed name, "VIVA", to consumers and considered that because the largest consumer of cooking oils in Canada was to be found amongst ethnic groups, the largest of which was Italian, it was important to employ a name for the proposed new cooking oil which would satisfy the English, French and Italian segments of the Canadian population. The test was also designed to determine the acceptability of the name "VIVA" to varying age and economic groups. Accordingly the test was conducted with a sample of 405 consumers, 205 in the province of Quebec and 200 in Toronto. Of the persons tested in Toronto 100 were Italian. The persons tested were classified according to age (under and over 35 years) and family income (under and over $5,000.00). The report by Louis Cheskin Associates to the Appellant was received by the Appellant in September of 1963. . . .

14. On August 21, 1963 the Registrar of Trade Marks informed the Appellant's solicitor that the proposed mark "VIVA" was considered to be confusing with registered trade mark number 126932, the property of Power Super Markets Limited . . .

15. During the month of August 1963 the Appellant expended $4,777.13 with respect to:

(a) services performed by Stewart & Morrison Limited for container and label design, and

(b) services performed by Baker Advertising Agency Limited for television commercials to be used to market the Appellant's new cooking oil, "VIVA".

16. During October of 1963 the Appellant expended $175.00 for services performed by Colour Research Institute with respect to a design for the proposed "VIVA" label.

17. In November of 1963 the Appellant approached officers of Power Super Markets Limited with a view to obtaining the consent of Power Super Markets Limited to the registration by the Appellant of the mark "VIVA".

18. In November of 1963 the Appellant again retained Louis Cheskin Associates to conduct further research with respect to the Appellant's plans for marketing "VIVA" cooking oil. . . .

19. During November of 1963 the Appellant expended the following sums in connection with the proposed launching of "VIVA" cooking oil in the market place:

Colour Research Institute for container and label design	$ 4,870.00
Baker Advertising Agency Limited for television commercials	859.82
Stewart & Morrison Limited for container and label design	1,952.22
Louis Cheskin Associates for market research	3,660.00
TOTAL	$11,342.04

20. On or about December 2nd, 1963 the Registrar of Trade Marks sent to Power Super Markets Limited a notice of the Appellant's application for registration of "VIVA".

21. During December of 1963 the Appellant expended $1,320.00 for services performed by Stewart & Morrison Limited with respect to the design of "VIVA" labels, shipping containers and advertising material and salesmen's kits.

22. On or about January 3rd, 1964 Power Super Markets Limited filed with the Registrar of Trade Marks a statement of opposition to registration of the trade mark "VIVA".

23. During January, 1964 the Appellant expended $2,525.00 for services performed by Colour Research Institute for ocular testing on Brand X display material and by Stewart & Morrison Limited with respect to the design of "VIVA" in shipping containers and advertising display material.

24. In February of 1964 Mr. A. S. Cummings, Vice-President of the Appellant, met with Mr. Leon Weinstein, an official of Power Super Markets Limited, and as a result of the meeting an agreement was entered into whereby Power Super Markets Limited would withdraw its opposition to registration by the Appellant of the trade mark "VIVA" in consideration of payment by the Appellant of the sum of $15,000.00 upon registration of the trade mark. . . .

25. During February of 1964 the Appellant expended $1,425 00 for services performed by Stewart & Morrison Limited in respect of tests on "VIVA" label designs and the preparation of "VIVA" sales and advertising materials. The Appellant also expended $1,836.00 for colour association tests performed by the Colour Research Institute.

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26. During March of 1964 the Appellant expended the following sums in connection with the launching of "VIVA" cooking oil in the market place:

(a) Stewart & Morrison Limited for containers and label designs	$ 1,050.00
(b) Consolidated Glass Company Limited for containers	5,599.58
(c) Miscellaneous	2,026.75

27. Pursuant to the agreement . . . Power Super Markets Limited withdrew its objection to the Appellant's application for the trade mark "VIVA" and on May 1st, 1964 the Appellant was registered as owner of the trade mark "VIVA" under registration number 135609 in respect of edible soya bean oil. . . . The $15,000.00 payment was released to Power Super Markets Limited on or about May 13, 1964. Subsequently, the Appellant applied for amendment to the statement of wares covered by its said trade mark 135609 by deleting the words "edible soya bean oil" and substituting therefor the words "edible vegetable oils". On 28 December, 1964 the Registrar of Trade Marks advised the Appellant that such application had been granted and the statement of wares had been amended. . . .

28. In April of 1964 "VIVA" cooking oil was test marketed and sales were made in the London and Calgary areas.

29. During April 1964 the Appellant incurred the following expenses:

(a) Colour Research Institute for container and label design	$ 165.00
(b) Baker Advertising Agency Limited for television commercials	$51,915.15
Total	$52,080.15

In effect, in the course of putting a new product on the market, the appellant, in addition to spending money on market research, industrial designs and advertising, spent money on obtaining the registration of a trade mark that it was adopting for the new product; and that expenditure included this amount of $15,000 that it paid to induce another company to drop its opposition to such registration being granted to it.

No question is raised by the respondent as to whether the amount of $15,000 was laid out for the purpose of earning the income from the appellant's business (section 12(1)(*a*))[1] or as to the reasonableness of the amount so

[1] 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,

laid out.[2] The only question that I have to consider is whether the deduction of the payment is prohibited by section 12(1)(*b*) because the payment was a payment "on account of capital". The respondent says that it was such a payment and the appellant says that it was not. I have to reach a conclusion this morning as to which of these two contentions is correct.

I start from the basis indicated by Fauteux, J., delivering the judgment of the Supreme Court of Canada in *M.N.R. v. Algoma Central Railway*,[3] where he says:

> Parliament did not define the expressions "outlay . . . of capital" or "payment on account of capital". There being no statutory criterion, the application or non-application of these expressions to any particular expenditures must depend upon the facts of the particular case. We do not think that any single test applies in making that determination and agree with the view expressed, in a recent decision of the Privy Council, *B.P. Australia Ltd. v. Commissioner of Taxation of the Commonwealth of Australia*, [1966] A.C. 224, by Lord Pearce. In referring to the matter of determining whether an expenditure was of a capital or an income nature, he said, at p. 264:
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> > The solution to the problem is not to be found by any rigid test or description. It has to be derived from many aspects of the whole set of circumstances some of which may point in one direction, some in the other. One consideration may point so clearly that it dominates other and vaguer indications in the contrary direction. It is a commonsense appreciation of all the guiding features which must provide the ultimate answer.

For the purpose of the particular problem raised by this appeal, I find it helpful to refer to the comment on the "distinction between expenditure and outgoings on revenue account and on capital account" made by Dixon J. in *Sun Newspapers Ltd. et al. v. Fed. Com. of Taxation*[4] at page 359, where he said:

> The distinction between expenditure and outgoings on revenue account and on capital account corresponds with the distinction between the business entity, structure, or organization set up or established for the earning of profit and the process by which such an organization operates to obtain regular returns by means of regular outlay, the difference between the outlay and returns representing profit or loss.

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[2] 12. (2) In computing income, no deduction shall be made in respect of an outlay or expense otherwise deductible except to the extent that the outlay or expense was reasonable in the circumstances.

[3] [1968] S.C.R. 447 at p. 449; [1968] C.T.C. 161 at p. 162.

[4] (1938) 61 C.L.R. 337.

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In other words, as I understand it, generally speaking,

(a) on the one hand, an expenditure for the acquisition or creation of a business entity, structure or organization, for the earning of profit, or for an addition to such an entity, structure or organization, is an expenditure on account of capital, and

(b) on the other hand, an expenditure in the process of operation of a profit-making entity, structure or organization is an expenditure on revenue account.

Applying this test to the acquisition or creation of ordinary property constituting the business structure as originally created, or an addition thereto, there is no difficulty. Plant and machinery are capital assets and moneys paid for them are moneys paid on account of capital whether they are

(a) moneys paid in the course of putting together a new business structure,

(b) moneys paid for an addition to a business structure already in existence, or

(c) moneys paid to acquire an existing business structure.

In my opinion, however, from this point of view, there is a difference in principle between property such as plant and machinery on the one hand and goodwill on the other hand. Once goodwill is in existence, it can be bought, in a manner of speaking, and money paid for it would ordinarily be money paid "on account of capital". Apart from that method of acquiring goodwill, however, as I conceive it, goodwill can only be acquired as a by-product of the process of operating a business. Money is not laid out to create goodwill. Goodwill is the result of the ordinary operations of a business that is so operated as to result in goodwill. The money that is laid out is laid out for the operation of the business and is therefore money laid out on revenue account.

Basically, as I understand it, a trade mark or trade name is merely one facet of the goodwill of a business. A trade mark or trade name is a mark or name which distinguishes the businessman's wares or services from those of others.

It so distinguishes his goods or services because, by virtue of his business operations, including the use of the name or mark, his goods or services have become distinct from those of others in the public mind. That was certainly so in the period when trade marks depended exclusively for their legal protection on the legal action for the tort of passing off. In my view, that basic commercial or business fact remains unchanged by any of the different statutory schemes that have been adopted to give greater legal protection to the public and to honest business men against practices whereby one businessman's goods or services can be passed off as those of another. I do not overlook the fact that statutory rights are now conferred on a person who obtains registration of a trade mark or the fact that registration can be obtained of a "proposed" mark. Such rights are, however, dependent on a complicated scheme of statutory conditions designed, as I understand them, to facilitate the provision of legal protection to members of the public and to business men who, by their business operations, have caused their goods or services to be distinguished by specific marks as against persons who would otherwise be able to take advantage of the confidence the public has acquired in such marks. In my view, a trade mark that actually distinguishes is, even under the statutory scheme, a result that flows from the current operations of a business and it follows, as I have already indicated, that the moneys laid out in the operations that incidentally give rise to trade marks are moneys laid out on revenue account. (I emphasize that moneys laid out to acquire a trade mark that is the creation of somebody else's business operations would, on the contrary, be moneys laid out on capital account.)

I have been speaking in relatively simple terms of a trader with a simple operation who buys and sells goods and, for that purpose, adopts some identifying mark. As the facts of this case illustrate, modern business is not conducted in such a simple way. In place of individual traders relying on their individual sagacity and judgment, there are huge corporations for whom each single decision becomes a major operation. Huge sums must be spent on market surveys before a decision can be made as to what product to market or as to what trade mark or trade name

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to adopt. Industrial designers are employed at great expense to choose a colour and design for a label. Lawyers, accountants and economists find employment in the highly complicated process that has replaced the decisions that an individual would have made "by the seat of his pants". Nevertheless, from the point of view of what are current business operations and what are capital transactions, as it seems to me, the distinction follows the same line.

In my view, the advertising expenses for launching the new product in this case were expenses on revenue account. I expressed a similar view in *Algoma Central Railway v. M.N.R.*[5] in a decision that was upheld on appeal.[6] As I indicated there, "According to my understanding of commercial principles . . . , advertising expenses paid out while a business is operating, and directed to attracting customers to a business, are *current* expenses". Similarly, in my view, expenses of other measures taken by a businessman with a view to introducing particular products to the market—such as market surveys and industrial design studies—are also current expenses. They also are expenses laid out while the business is operating as part of the process of inducing the buying public to buy the goods being sold.

It remains to consider expenses incurred by a businessman, during the course of introducing new products to the market, to obtain the additional protection for his trade mark that is made available by trade mark legislation. A new mark adopted and used in the course of marketing a product gradually acquires the protection of the laws against passing off (assuming that it is, in fact, distinctive). This is something that is an incidental result of ordinary trading operations. Additional expenditure to acquire the additional protection made available by statute law seems to me to be equally incidental to ordinary trading operations. It follows that, in my view, the fees paid to trade mark lawyers and to the trade mark office are deductible. In this case, no submission was presented to me as to any principle whereby I should distinguish between the ordinary costs of acquiring trade mark registration and the

[5] [1967] 2 Ex. C.R. 88

[6] [1968] S.C.R. 447, [1968] C.T.C. 161.

$15,000 payment that, in this case, was necessary in the judgment of the appellant to obtain registration of its trade mark "VIVA", and I have been able to conceive of no such principle.

What the respondent does say is that the payment of $15,000 must be disallowed as being a payment "on account of capital", and he relies on the "usual test" to which I referred in *Algoma Central Railway v. M.N.R., supra,* at page 92 as follows:

> The "usual test" applied to determine whether such a payment is one made on account of capital is, "was it made 'with a view of bringing into existence an advantage for the enduring benefit of the appellant's business'"? See *B.C. Electric Ry. Co. Ltd. v. Minister of National Revenue,* [1958] S.C.R. 133, per Abbott J. at pages 137-8, where he applied the principle that was enunciated by Viscount Cave in *British Insulated and Helsby Cables, Ltd. v. Atherton, supra,* and that had been applied by Kerwin J., as he then was, in *Montreal Light, Heat & Power Consolidated v. Minister of National Revenue,* [1942] S.C.R. 89 at 105.

The respondent says that the payment of $15,000 was made "with a view of bringing into existence an advantage for the enduring benefit of the appellant's business," because it made the payment in order to acquire a registered trade mark with all the statutory rights to which the owner of a registered trade mark is entitled. Looking only at the *Trade Marks Act,* there is much force in this contention. However, in distinguishing between a capital payment and a payment on current account, in my view, regard must be had to the business and commercial realities of the matter. When the intricate conditions of the *Trade Marks Act* are properly understood, they operate so that the statute only provides protection for a trade mark that is distinctive of the owner's wares or services. If it does not distinguish them, the registration is invalid (section 18), and the protection afforded by section 19 does not apply. The situation is, therefore, that if, as a result of the ordinary current operations of a business, a trade mark is distinctive, the action of passing off (and section 7 of the *Trade Marks Act*) operates to give automatic protection; and additional protection can be obtained by registration. The trade mark, as an advantage for the enduring benefit of the business, is the product of the current operations of the business and is

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not the result of registration. Registration merely facilitates the businessman in enforcing the rights that accrued to him from his business operations. Either "VIVA" will be found, if it is ever tested, to have become distinctive of the appellant's wares by virtue of its trading operations, or its registration will be found to be invalid. Mere registration is an empty right if it is not based on a trade mark that has business or commercial reality as an incidental consequence of the current operations of the business. In my view, therefore, the trade mark in question was an "advantage for the enduring benefit of the...business", if it is such an advantage, was not acquired by the payment of $15,000.

Putting my view another way, it is that, while a trade mark once it becomes a business or commercial reality is a capital asset of the business giving rise to it, just like goodwill, of which it is merely a concrete manifestation, a trade mark is not a capital asset that has been acquired by a payment made for its acquisition, but is a capital asset that arises out of, and can only arise out of, current operations of the business; and registration of a trade mark does not create a trade mark that is such a business or commercial reality, but is merely a statutory device for improving the legal protection for it.

The appeal will be allowed and the assessment will be referred back to the respondent for reassessment on the basis that the sum of $15,000 referred to in paragraph 13 of the Notice of Appeal is deductible in computing the income of the appellant for the 1964 taxation year. The appellant will have its costs in an amount which it is agreed should be $938.65.