



SENTINEL HILL ENTERTAINMENT
CORPORATION

May 20, 2008

Investor First Name, Investor Last Name
Address, Address
City, Province Postal Code

**RE: Sentinel Hill 1998 Master Limited Partnership
Update: Canada Revenue Agency - Appeal to the Tax Court of Canada
ACTION REQUIRED BY LIMITED PARTNERS**

We are writing this letter to the Limited Partners of Sentinel Hill 1998 Master Limited Partnership (the "Partnership") as part of our ongoing reporting to you concerning the activities of the Partnership and in particular, the appeal on behalf of Limited Partners to the Tax Court of Canada of the reassessment of the Partnership by the Canada Revenue Agency ("CRA") and the decision of the Partnership to also commence civil proceedings against the CRA and certain of its officials.

Our last correspondence to you on this matter was on October 27, 2006. At that time, we advised you that the CRA had decided to send Notices of Confirmation of the reassessments of the Limited Partners and that these Notices needed to be appealed to the Tax Court of Canada. We urged you to sign a form provided to you with our letter authorizing the law firm Thorsteinssons LLP (a nationally recognized firm of tax specialists) to file a Notice of Appeal to the Tax Court of Canada on your behalf. We are pleased that Limited Partners responded positively to our urging, and the Appeal has been underway since the beginning of 2007.

We further advised you that we would be contacting you after receipt of the federal Government's Notice of Reply (essentially a statement of defense to the Notice of Appeal). While remarkably this Notice of Reply has still not been sent by the CRA, we feel it is appropriate that we contact you at this time to bring you up to date on recent developments in respect of this matter and to advise you of our proposed future course of action.

Notice of Appeal and Settlement Proposal

After filing the Notice of Appeal, and in the hope of resolving the Appeal before litigation commenced, we instructed Thorsteinssons to make another proposal (subsequent to the one discussed in the October 27, 2006 letter) to settle the case by agreeing to a reduction in the deductible amounts in question. This settlement would have resulted in a corresponding reduction in the deferred taxable capital gain payable by you in 2009. Thorsteinssons and we were optimistic that this offer, which was more generous to the CRA than the settlement which the CRA accepted for the Sentinel Hill 2000 Partnership, would be agreed to.

The offer was made only after much consideration by the General Partner, deliberation between the General Partner and Thorsteinssons and a sampling of views from some of the Limited Partners. It in no way reflected our views as to the merit of the CRA's position, nor the integrity of the transactions, which the Limited Partners entered into in 1998. Some factors considered were the protracted nature of tax appeals (which we believe may drag on for another 3 years), the fact that Limited Partners were expecting the transaction to be complete by the spring of 2009, and the general fatigue of Limited Partners with the ongoing CRA matter. The offer was made subject to the approval of each Limited Partner.

To our disappointment, but not surprise, the CRA rejected our proposal out-of-hand and immediately commenced the tax litigation action. Rather than filing its Notice of Reply to the Limited Partnership's Notice of Appeal so that a court date could be set down, the CRA's first step was to file a motion in Tax Court to deny the partners of the 1998 Limited Partnership the ability to refer to the 1998 advance income tax rulings on the basis that the rulings were not relevant. We instructed Thorsteinssons to oppose this motion and we filed an affidavit in support of our position. On April 12, 2007 and again on October 16, 2007, Robert Strother of Sentinel Hill was cross-examined on this affidavit by federal government lawyers. The motion was heard by Chief Judge Bowman of the Tax Court on December 4, 2007.

Decision on the Motion

The decision of Chief Judge Bowman was delivered on December 19, 2007. The CRA's motion to deny the partners of the 1998 Limited Partnership the right to refer to the 1998 advance rulings was dismissed with costs payable by the CRA. The CRA was ordered to file its Reply (i.e., commence the tax litigation in earnest) within 30 days.

The reasons of the Chief Judge are a powerful rejection of the CRA's position and are noteworthy in the following respects:

First, on the question of the relevance of the rulings, Bowman C.J. held that the matter was one which should be determined by a trial judge and not summarily dismissed in a

chambers motion (in the following quotes, the “respondent” is the CRA and the “appellant” is Sentinel Hill):

“If the respondent wishes to challenge the facts alleged, a section 53 motion is not the place in which to do so. It is at trial where a judge hearing the evidence can determine the correctness, relevancy and weight to be assigned to the evidence adduced in support of the allegations”. (Paragraph 6 of the Judgment)

“Whether I agree that the factual components of estoppel exist or whether the advance rulings constitute agreements is not germane to the disposition of these motions. The appellants should be entitled to advance such arguments at trial on the basis of all the evidence.” (Paragraph 11)

Second, as to the binding nature of an advance income tax ruling, quoting from a prior decision of the Chief Judge:

“I leave aside entirely the question of advance rulings which form so important and necessary a part of the administration of the Income Tax Act. These rulings are treated by the Department of National Revenue as binding. So far as I am aware no advance ruling that has been given to a taxpayer and acted upon has ever been repudiated as against the taxpayer to whom it was given. The system would fall apart if he ever did so.” (Paragraph 8)

Third, as to the tactics of the CRA in using “procedural skirmishes” to delay the process of tax litigation and thereby raise the costs to taxpayers, including motions to strike tax payers’ arguments and pleadings as “scandalous, frivolous or vexatious or an abuse of the process of the Court”:

“However much jurisprudence may surround the words ‘scandalous, frivolous or vexatious, or abuse of the process of the Court’, they are nonetheless strong, emotionally charged and derogatory expressions denoting pleading that is patently and flagrantly without merit. Their application should be reserved for the plainest and most egregiously senseless assertion – as for example in *William Shawn Davitt v. The Queen*, 2001 DTC 702. Where senior and experienced counsel advances a proposition of fact or law in a pleading that merits serious consideration by a trial judge, it is at least presumptuous and at most insulting and offensive to force counsel to face the argument that the position is so lacking in merit that it does not even deserve to be considered by a trial judge. It is a deplorable tactic for the Crown, as soon as it sees legal argument that it does not like, to move to strike. As I said in *Sackman v. The Queen*, 2007 TCC 455, it is this sort of skirmishing that is putting tax litigation out of the reach of ordinary people. I do not wish to see this court turned into a forum for procedural manoeuvring. I repeat what was said in *Satin Finish Hardwood Flooring (Ontario) Limited v. The Queen*, 96 DTC 1402 at 1405:

‘There was no justification for bringing this motion. It serves no purpose within the context of this litigation. The time that has been spent on this exercise in procedural

oneupmanship would have been better spent, following the filing and serving of a reply, in conducting an examination for discovery in which the evidentiary basis of the appellant's challenge to the assessment could readily have been ascertained. The rules of this court, which are designed to facilitate, not impede, the expeditious determination of fiscal disputes, should not be used to carry out unproductive procedural maneuvering.” (Paragraph 11)

Fourth, as to the notion that the CRA is entitled to repudiate advance rulings:

“The respondent's position is ambivalent. I asked counsel if he was saying that advance rulings were not binding or that the appellants had not conformed to them. His answer was “Both”. If the argument is that they do not apply to the appellants or that their terms had not been complied with, this is a factual matter that contradicts the allegations in the notices of appeal. It cannot be raised on these motions. It must be decided on evidence at trial. If the respondent is now seeking to establish that advance rulings can be repudiated by the Minister after decades of reliance by taxpayers upon them, this proposition, which would startle most practitioners, should be tested in a full trial and not a preliminary motion. This preliminary motion is certainly not the time or place to discuss the complex issues arising out of the Minister's remarkable position. The ruling process, which was created by Revenue Canada and has been enormously beneficial to taxpayers in creating certainty in predicting the tax consequences of commercial transactions, constitutes a fundamental cornerstone of Canadian tax administration. The idea that a motions judge could, on the basis of a one hour argument without evidence, demolish one of the essential underpinnings of our system is, quite frankly, appalling.” (Paragraph 12)

“The magnitude of this question transcends the boundaries of a preliminary motion and is indeed of a greater importance in the field of taxation than any I have seen in many years.” (Paragraph 13)

CRA's Response to the Decision

We acknowledge and understand that the Limited Partners are very frustrated with this situation, as are we. We have previously communicated to you that we feel that the CRA has been and continues to be disingenuous in its dealings with Sentinel Hill limited partnerships. We don't appear to be alone in this view. In another recent Tax Court of Canada case (unrelated to Sentinel Hill) the judge was highly critical of the tactics of the federal government lawyer representing the CRA and decried the “win at all costs” approach of the CRA. The Tax Court noted that the government lawyers (and by implication the CRA) are fulfilling a public duty; they should press their case firmly but fairly, and perform their duty with an ingrained sense of the dignity, the seriousness and the justness of judicial proceedings.

We take comfort in the Chief Judge of the Tax Court's characterization of the CRA's tactics as **“at least presumptuous and at most insulting and offensive”, “deplorable” and “appalling.”**

Having defeated the CRA's motion, we expected the CRA to comply with the Tax Court's order to file a Notice of Reply so that the substantive issues for the 1998 appeal could be heard in 2008. Astonishingly, in light of the Chief Judge's comments on the CRA's tactics, the CRA has advised that it will appeal Chief Judge Bowman's decision to the Federal Court of Appeal.

We sought and are in receipt of an opinion letter as to the merits of the tax court appeal from Thorsteinssons dated October 29, 2007. After a review of the issues, Thorsteinssons concluded that, while success cannot be assured, there are very good grounds to “substantially or entirely reverse the reassessments by proceeding to Tax Court.”

To date, the Sentinel Hill General Partners have funded all third party expenses, including significant legal fees, lobbyist expenses, and Limited Partner filing fees associated with the audits, and appeals of the 1998, 1999, 2000 and 2001 partnerships. These expenses approximate \$2,800,000. The shareholders of Sentinel Hill Entertainment Corporation (Paul Darc and Robert Strother) are continuing to fund the Tax Court proceedings of the Partnership at this time.

Action required by Limited Partners – Letter of Authority

We have recently received legal advice that while the 1998 Limited Partnership Agreement authorizes the General Partner to conduct the affairs of the Partnership as it has to date, it does not contemplate the current situation of potentially representing each of the Limited Partners in their individual capacity, in tax litigation. Therefore, it is necessary for us to seek authority and instructions from the Limited Partners regarding the conduct of the litigation, including entering into a binding settlement, if any. We have received confirmation from the CRA that they will proceed with a single “test case” for 1998. In order for the General Partner to represent you, please complete and mail to us, in the enclosed self addressed envelope, the attached letter of authority.

Action required by Limited Partners – Civil Action

In addition to the Tax Court proceedings, we have received legal opinions from a leading litigation boutique, Groia & Company Professional Corporation, that the Partnership has the basis for a good cause of civil action against the CRA and some of its senior officials. The root of these actions is the disregard by the CRA of the Advance Income Tax Rulings which deal with much of the substance of the reassessments, and the course of conduct of certain of the CRA officials during the ruling application process and the audit. CRA's track record and Groia & Company Professional Corporation's

assessment suggests that the civil litigation will likely be a protracted matter and, though there is a good cause of action, the outcome cannot be determined at this time.

We believe it is in the best interest of the 1998, 1999 and 2001 Partnerships to file civil suits against the CRA to be initiated concurrently with (but independent of) the tax court proceedings. Such suits are beyond our mandate as general partners and, as such, we request a contribution from the Limited Partners to fund the preparation, filing and prosecution of these actions.

To fund this civil litigation, we are seeking a contribution of \$3.50 per Limited Partnership Unit for 1998 Limited Partners within 30 days of this letter. As you hold # Units, your contribution will be [\$]. We are seeking an equivalent contribution from 1999 and 2001 Limited Partners. If each partner makes their contribution, the aggregate of money collected from 1998, 1999 and 2001 Limited Partners will be sufficient to fund the civil litigation expenses and related expenses discussed above. Funds will be treated as a capital contribution, and Partnership expenses will be tax deductible. At the end of each year, the amounts will be included on the T5013A sent to you for your income tax return.

Please make your [\$] payment within 30 days to: Sentinel Hill 1998 Master Limited Partnership

The General Partner believes it is important to ensure that all Limited Partners make their contributions within 30 days of this letter. If sufficient numbers of the Limited Partners make their \$3.50 per Unit contributions, then the General Partner will proceed to retain Groia & Company Professional Corporation, who has agreed, once retained, to act for the General Partner in pursuing the civil claim. The individual Limited Partners would not be clients of Groia & Company Professional Corporation, but would receive updates on the progress of litigation from the General Partner and would be entitled to indirectly share in any recovery.

If insufficient Limited Partners make their \$3.50 per Unit contribution, then there will be insufficient funds to pursue the civil action against CRA. In this event, the civil action will not be pursued by the General Partner and your contribution will be returned to you. In this case, the General Partner will have exhausted its ability to act on behalf of the Partnership with respect to the civil claim. The claims that the Partnership or you may have may be lost in this circumstance.

Delivery of Contribution

Please forward a cheque for the requested contribution and the enclosed Memo in the self addressed prepaid envelope provided. Please ensure the cheque is addressed and payable to "Sentinel Hill 1998 Master Limited Partnership".

Based on the advice of Thorsteinssons, we remain optimistic that our prospects for substantial success in the tax litigation are very good. It is unfortunate that the matter could not be resolved through administrative appeal at the CRA or, at this time, by negotiation. We continue to stand behind the Limited Partners and will dedicate our time and resources to the favourable resolution of this matter. If you wish to receive a copy of Chief Justice Bowman's Judgment in full, please make that request to Eau-Vive Rivest, Manager of Investor Relations at erivest@sentinelhill.com.

Yours truly,

SENTINEL HILL PRODUCTIONS CORPORATION

Per:

Letter of Authority

The undersigned, being a limited partner of the Sentinel Hill 1998 Master Limited Partnership (the "Partnership") hereby authorizes and instructs Sentinel Hill Productions Corporation (Sentinel Hill), the general partner of the Partnership to take any and all actions in respect of the reassessment by the Canada Revenue Agency ("CRA") of the undersigned in respect of losses claimed by the undersigned for income tax purposes in respect of the business and affairs of the Partnership, including:

- engaging and instructing legal counsel in respect of an appeal of the reassessment and all matters related thereto;
- providing evidence and documentation to legal counsel to enable legal counsel to prosecute the appeal of the reassessment;
- proposing and negotiating the terms of any settlement of the reassessment with CRA or responding to any terms of any settlement proposed by CRA;
- agreeing to the terms of, and entering into any agreement with CRA in respect of a compromise or settlement of the reassessment;
- obtaining and receiving all documents and other materials provided by CRA to undersigned in respect of the appeal of the reassessment; and
- doing all such other things that in the opinion of Sentinel Hill are consistent with prosecution of the appeal of the reassessment.

And the undersigned authorizes Sentinel Hill to do any of the foregoing in the name of the undersigned, and to execute and deliver all such documents and instruments in the name of the undersigned as may be necessary or desirable to carry out the intention of this letter of authority.

Dated the ____ day of _____, 2008

Signature of Limited Partner

Witness Signature

Print Name of Witness

Investor First Name, Investor Last Name
Address, Address
City, Province Postal Code

MEMO

Date:

To:

Sentinel Hill 1998 Master Limited Partnership
218 – 179 Davie Street
Vancouver, BC V6Z 2Y1

From:

Investor First Name, Investor Last Name
Address, Address
City, Province Postal Code

Please find enclosed, my payment for [\$] for deposit in the Sentinel Hill 1998 Master Limited Partnership as my contribution to support the civil litigation.