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Ministère de la Justice  
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Name / Nom: Warren J.A. Mitchell  
Thorsteinssons

Name / Nom: Ryan R. Hall  
Department of Justice, Canada

Address /  
Adresse:

**COPY DRD.**

Tax Law Services Section  
Bank of Canada Building  
East Tower  
234 Wellington Street, Room 922  
Ottawa, Ontario  
K1A 0H8

Fax # / No du télécopieur:  
(604) 688-4711

Tel. No. / No de Tél:

Fax # / No du télécopieur:  
(613) 941-2293

Tel. No. / No de Tél:  
(613) 941-2292

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# of Pages:

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Date:

April 20<sup>th</sup>, 2010

Time



Department of Justice  
Canada

Ministère de la Justice  
Canada

Tax Law Services Section  
Bank of Canada Bldg., East Tower  
234 Wellington Street  
Ottawa, Ontario  
K1A 0H8

Section des Services du droit fiscal  
Édifice Banque du Canada, Tour Est  
234, rue Wellington  
Ottawa, Ontario  
K1A 0H8

Phone: (613) 957-4816  
Fax: (613) 941-2293

April 20, 2010

BY FAX

**WITHOUT PREJUDICE**

Warren J. A. Mitchell  
Thorsteinssons  
Barristers and Solicitors  
P.O. Box 49123, 3 Bentall Centre  
27th Floor - 595 Burrard Street  
Vancouver, British Columbia  
V7X 1J2

Dear Sir:

**Re: Sentinel Hill Productions IV Corporation, member of SHAAE (2001) Master Limited Partnership v. Her Majesty The Queen  
Court Number: 2009-2248(IT)G - Justice File: 3-707094 et al. ("2001 appeals")  
Robert C. Strother v. Her Majesty The Queen  
Court Number: 2007-329(IT)G - Justice File: 3-705321 et al. ("1998 appeals")**

We write in response to the settlement proposals forwarded by Messrs. Strother and Darc on February 12, 2010, a copy of which is attached. You will note that the settlement proposals forwarded by Messrs. Strother and Darc address the 2001 appeals and the 1998 appeals. We will respond to both proposals.

**Settlement Proposal: 1998 appeals**

The proposal for the 1998 appeals, as we understand it, would simply reduce the losses claimed on a percentage basis comparable to the percentage disallowance reflected in other Sentinel Hill settlements. While the Canada Revenue Agency remains open to a resolution of these appeals, the proposal advanced by Messrs. Strother and Darc is neither well-founded in law nor acceptable. The Canada Revenue Agency therefore rejects the offer.

If the appellants wish to present a proposal based in acceptable tax law principles, the Canada Revenue Agency will give it appropriate consideration.

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**Settlement Proposal: 2001 appeals**

The Canada Revenue Agency has also considered the settlement proposal for the "2001 appeals" contained in the letter of Messrs. Strother and Darc. The Canada Revenue Agency rejects the offer to settle. However, with respect to the 2001 appeals the Canada Revenue Agency is, on a without prejudice basis, prepared to make a counter-offer to settle.

In particular, the respondent offers to settle the appeals by issuing a redetermination pursuant to subsection 169(3) of the *Income Tax Act* in accordance with the following terms:

1. The Minister shall issue a redetermination of SHAAE (2001) Master Limited Partnership for the fiscal periods under appeal disallowing, *in total*, \$94,375,407, such being the disallowance of the originally disallowed Unreasonable Expenses in the total amount of \$101,899,530 less the Withholding Tax on the Studio Fees and Interest in the aggregate amount of \$7,524,123. Specifically, the redetermination would disallow the following:

Fiscal period	Losses disallowed per proposed redetermination	Losses disallowed per disputed determination
2001	\$68,103,756	\$136,101,880
2002	\$26,271,651	\$43,784,373
Totals	\$94,375,407	\$179,886,253

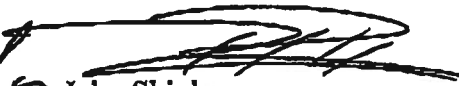
2. The enclosed Notices of Discontinuance with respect to the Tax Court of Canada Appeals numbered 2009-2248(IT)G and 2009-2247(IT)G shall be executed and forwarded to counsel for the respondent.
3. Upon issuance of the Notice of Redetermination referred to in paragraph 1, counsel for the respondent shall file the Notices of Discontinuance referred to in paragraph 2 above with the Tax Court of Canada and send filed copies to the appellants' address for service.
4. The appellant shall not file a Notice of Objection, Notice of Appeal or otherwise challenge the determination referred to in paragraph 1.
5. Without the prior written approval of the Canada Revenue Agency, the terms of this settlement will not be disclosed to any third party except as required by applicable law, and, in the event such disclosure is required by applicable law to

-3-

such third party, the Canada Revenue Agency will be notified of such disclosure prior to such disclosure being made.

6. Sentinel Hill Productions IV Corporation shall sign the proposed minutes of settlement contemplated by this offer in its capacity as the general partner of, and on behalf of, each of SHAAE (2001) Master Limited Partnership, Sentinel Hill No. 207 Limited Partnership and the remaining 72 production limited partnerships listed in the annex hereto (the "Remaining PLPs").
7. SHAAE (2001) Master Limited Partnership, Sentinel Hill No. 207 Limited Partnership and the Remaining PLPs are entitled to no further relief.
8. The parties will bear their own costs.

Yours truly,



John Shipley  
Senior General Counsel

Encls.

c.c. R. Carvalho, I. Nwachukwu, R. Hall

**ANNEX****Remaining Production Limited Partnerships or PLPs**

Catfight Productions 2 Limited Partnership  
Ocularis Limited Partnership  
Sentinel Hill No. 28 Limited Partnership  
Sentinel Hill No. 32 Limited Partnership  
Sentinel Hill No. 34 Limited Partnership  
Sentinel Hill No. 36 Limited Partnership  
Sentinel Hill No. 40 Limited Partnership  
Sentinel Hill No. 51 Limited Partnership  
Sentinel Hill No. 52 Limited Partnership  
Sentinel Hill No. 58 Limited Partnership  
Sentinel Hill No. 68 Limited Partnership  
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- Sentinel Hill No. 255 Limited Partnership
- Sentinel Hill No. 258 Limited Partnership
- Sentinel Hill No. 280 Limited Partnership

2009-2248(IT)G

**TAX COURT OF CANADA**

BETWEEN:

**SENTINEL HILL PRODUCTIONS IV CORPORATION, MEMBER OF SHAAE  
(2001) MASTER LIMITED PARTNERSHIP**

Appellant

- and -

**HER MAJESTY THE QUEEN**

Respondent

**NOTICE OF DISCONTINUANCE**

**TAKE NOTICE THAT** the appellant discontinues its appeal from Notices of Determination issued on March 29, 2005 and March 30, 2005 for the appellant's fiscal periods ended December 31, 2001 and December 31, 2002, respectively.

DATED at the City of Vancouver, British Columbia, this            day of  
2010.

---

Warren J. A. Mitchell  
Counsel for the appellant

The respondent consents to the discontinuance of the appellant's appeal without costs.

DATED at the City of Ottawa, Ontario, this            day of            , 2010.

---

John Shipley  
Counsel for the respondent

**TO:**            The Registrar  
                 Tax Court of Canada  
                 200 Kent Street, 4<sup>th</sup> Floor  
                 Ottawa, Ontario  
                 K1A 0M1



2009-2247(IT)G

**TAX COURT OF CANADA**

BETWEEN:

**SENTINEL HILL PRODUCTIONS IV CORPORATION, MEMBER OF  
SENTINEL HILL NO. 207 LIMITED PARTNERSHIP**

Appellant

- and -

**HER MAJESTY THE QUEEN**

Respondent

**NOTICE OF DISCONTINUANCE**

**TAKE NOTICE THAT** the appellant discontinues its appeal from Notices of Determination issued on March 29, 2005 and March 30, 2005 for the appellant's fiscal periods ended December 31, 2001 and December 31, 2002, respectively.

DATED at the City of Vancouver, British Columbia, this            day of            ,  
2010.

---

Warren J. A. Mitchell  
Counsel for the appellant

The respondent consents to the discontinuance of the appellant's appeal without costs.

DATED at the City of Ottawa, Ontario, this            day of            , 2010.

---

**John Shipley**  
Counsel for the respondent

**TO:**            The Registrar  
                 Tax Court of Canada  
                 200 Kent Street, 4<sup>th</sup> Floor  
                 Ottawa, Ontario  
                 K1A 0M1



SENTINEL HILL VENTURES  
CORPORATION

**FAX TRANSMISSION**

**DATE:** February 12, 2010

<b>TO:</b>	Mr. John Shipley	<b>FAX NO.:</b> 613-941-2293 <b>TEL NO.:</b>
<b>FROM:</b> <b>DIRECT TEL:</b> <b>EMAIL:</b>	Sharon Dhesi 604.692.2403 sdhesi@magnoliacapital.ca	<b>PAGES SENT: 3</b> <i>Including fax cover page.</i>

**MESSAGE**

On behalf of Paul Darc and Robert Strohler, please find to follow an outline of a full settlement proposal for the 2001 Appeal and the 1998 Appeals.

Regards,

Sharon Dhesi  
Executive Assistant  
Magnolia Capital Corporation

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February 10, 2009

**VIA FACSIMILE (613) 941-2293**

**WITHOUT PREJUDICE**

Mr. John Shipley  
General Counsel  
Tax Law Services  
Department of Justice  
234 Wellington Street  
Ottawa, ON  
K1A 0H8

Dear Sir:

**Re: SHAAE (2001) Master Limited Partnership v. The Queen (the "2001 Appeal");  
Investors in Sentinel Hill 1998 Master Limited Partnership (the "1998 Appeals")**

Further to our meeting of January 27, 2010 and our telephone conversation of February 8, 2010 with Mr. John Crowley, we write to outline a full settlement proposal for the 2001 Appeal and the 1998 Appeals. This offer is made on a "without prejudice" basis and applies only if and to the extent that your client accepts the terms outlined herein for both groups of appeals.

**Background**

The Sentinel Hill group structured a number of film transactions over a four year period from 1998 to 2001. All were challenged by the CRA to a greater or lesser extent. We have, however, successfully resolved the 1999 and 2000 Sentinel Hill transactions without litigation.

In light of the Rulings issued for the 1998, 2000 and 2001 transactions, we, and the 1998 and 2001 investors, view the 2000 Sentinel Hill settlement as the benchmark for the resolution of the 1998 and 2001 Sentinel Hill transactions.

The terms on which the 2000 Sentinel Hill transaction – Sentinel Hill Alliance Atlantis Equicap Millennium Limited Partnership – was resolved was to reassess by agreement to deny 12.43% of the losses claimed in the first two years (amounting to \$54,250,000 of denied losses out of \$436,482,000 reported losses) and to defer the deduction of a further \$55,808,000 of Studio Fees over seven years on a 20-20-15-15-15-5-5 basis. The negotiated settlement was reached after a number of proposals were exchanged and resulted in a denial of approximately 40% of the deductions challenged by CRA. The allocation of the denied losses among various categories was made by agreement between the parties to the settlement and resulted solely from a "numbers based" negotiation.

### **Settlement Proposal: 2001 Appeal**

In order for a settlement to be palatable to the 2500+ investors in the 2001 Sentinel Hill transaction, we believe the 2001 Appeal must be resolved generally within the parameters of the negotiated settlement of the 2000 Sentinel Hill transaction (wherein 12.43% of reported losses were denied over the first two years).

The reported losses over the first two years of the 2001 Sentinel Hill transaction were \$392,000,000. For settlement purposes, the partnership would accept the disallowance of \$50,000,000 of the deductions comprising those losses (12.76%). In addition, the partnership would agree to treat the Studio Fees as the acquisition cost of a class 14 depreciable asset, fully depreciable at the same rate as in the 2000 settlement over seven years. Under this offer, the percentage of disallowed losses is slightly higher than under the 2000 Sentinel Hill settlement (12.74% versus 12.43%), but within a tolerance that we believe would be acceptable to the investors. Further, the settlement proposal, expressed as a percentage of challenged losses, compares favorably to the 2000 Sentinel Hill settlement.

The denied deductions would be applied proportionately across the 2001 and 2002 taxation years in the same proportion as the losses were reported.

From the CRA's perspective, settling the 2001 Sentinel Hill transaction now has the added benefit of ensuring that a capital gain is reported by investors in their 2011 taxation year. We could agree, as part of the settlement, to allow the CRA to review the draft partnership dissolution documents. This way, the CRA can ensure that the capital gains are satisfactorily realized.

### **Settlement Proposal: 1998 Appeals**

The 1998 Sentinel Hill transaction also had a Ruling, and thus we believe also ought to be resolved by reference to the 2000 Sentinel Hill settlement. Furthermore, the basis of the CRA's challenge to the 1998 losses is different than for the subsequent years' transactions. There were no fees or expenses in the 1998 Sentinel Hill transaction that the CRA viewed as "circular" - all such fees and expenses were paid in cash.

We believe that the 1998 investors could be persuaded to agree to a settlement determined by reference to the same percentage disallowance as in the 2000 Sentinel Hill settlement (12.43%). On that theory, of the \$28,991,890 in aggregate reported losses in the 1998 transaction, losses of \$3,603,692 would be disallowed pro rata among the 1998 investors.

Mr. Strother is an investor in 1998. Mr. Strother's father was also a 1998 investor, and Mr. Strother is the executor of his father's estate. Mr. Strother would agree on his own behalf and on behalf of his father's estate to this settlement. If the CRA agrees to this settlement, Mr. Strother would also recommend the settlement to the other 1998 investors.

In addition, we would correspond with the other 1998 investors who choose to accept the settlement in order to advise them of their recomputed capital gain on the dissolution of the 1998 partnership in 2008. If investors do not refile their 2008 returns to report the revised capital gain, the CRA still has the power to reassess the investors' 2008 taxation year either within the

"normal reassessment period" for 2008 or under the consequential reassessment rule in subsection 152(4.3) of the *Income Tax Act*.

**Other Matters**

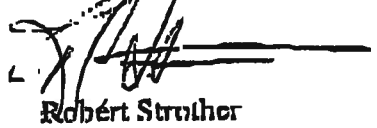
As part of the settlements, the CRA would also agree to favourably consider an interest waiver application to be submitted pursuant to subsection 220(3.1) of the *Income Tax Act* for a reasonable period of time (say 60 months) for both transactions.

We would also agree to keep the terms of any settlement confidential, on the same terms as the general partner was bound with respect to the settlement of the 1999 Sentinel Hill transaction.

**Next Steps**

We will contact Mr. Crowley during the first week of March, 2010 to receive a response to our proposal. We reiterate our desire to resolve the aforesaid matters by negotiation.

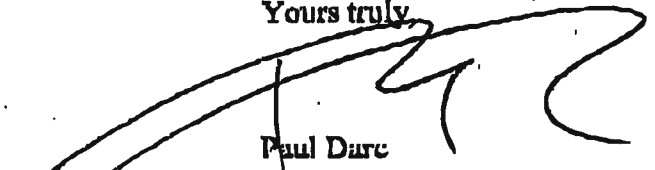
Yours truly,



Robert Struther

Director, Sentinel Hill Ventures Corp. &  
Sentinel Entertainment Corp  
Limited Partner, Sentinel Hill 1998

Yours truly,



Paul Durc

Director, Sentinel Hill Ventures Corp. &  
Sentinel Hill Entertainment Corp.

cc: Mr. John Crowley by fax 1-613-941-8088

cc: Mr. Robert Carvalho, Department of Justice (Vancouver) by fax 604-666-2214

cc: Thorsteinssons LLP - David Davies by fax 604-688-4711