Docket: 2007-329(IT)G

BETWEEN:

ROBERT STROTHER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Motion heard on common evidence with the motion in the appeal of *Sentinel Hill Productions IV Corporation, in its capacity as designated member of Sentinel Hill No. 207 Limited Partnership* (2009-2247(IT)G) and *Sentinel Hill Productions IV Corporation, in its capacity as designated member of Shaae (2001) Master Limited Partnership* (2009-2248(IT)G) on September 22, 2010 at Toronto, Ontario.

Before: The Honourable Gerald J. Rip, Chief Justice

Appearances:

Counsel for the Appellant:	Warren J.A. Mitchell David Davies
Counsel for the Respondent:	John Shipley Robert Carvalho

ORDER

Upon motion by the appellant for leave to make a motion to attack portions of the respondent's Reply to the Notice of Appeal, pursuant to Rule 8 of *Tax Court of Canada Rules* (*General Procedure*) ("the *Rules*");

And upon hearing what was alleged by the parties;

The appellant is granted leave to make a motion pursuant to Rule 53 of the *Rules*;

And upon motion by the appellant for an order pursuant to Rule 53 of the *Rules* striking out portions of the respondent's Reply to the Notice of Appeal;

The following portions of the Reply to the notice of appeal shall be struck:

1) paragraphs 1(e), 1(f), 1(g), 1(k), 1(n), 1(p), 2 to 15, 18, 20, 22, 26, 29, 46(c), 46(h), 46(q), 50(iii); and

2) The quotation marks and words within the quotation marks contained in paragraphs 38 to 42, 46(l), 46(o), 46(p), 46(s), 46(t)(i), 46(t)(ii), 46(t)(iii), 46(jj), 46(qq), 46(vv), 46(ggg) - Title, 46(iii), 46(nnn), 46(qqq), 46(ssss), 46(uuuu), 46(zzzz), 46(ccccc), 48.

The respondent may serve and file its Amended Reply in accordance with the reasons for order herein by June 30, 2011 and the appellant shall have 30 days thereafter to serve and file an Answer to the Amended Reply.

One set of costs shall be awarded to the appellants in the motions heard on common evidence with this motion. Counsel shall make submissions in writing with respect to whether costs shall be awarded on a solicitor-client basis by June 30, 2011 if they cannot agree on a fixed amount of costs in these motions.

Signed at Ottawa, Canada, this 12th day of May, 2011.

"Gerald J. Rip"

Rip C.J.

Citation: 2011 TCC 251
Date: 20110512
Docket: 2007-329(IT)G

BETWEEN:

ROBERT STROTHER,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2247(IT)G

BETWEEN:

SENTINEL HILL PRODUCTIONS IV CORPORATION,
IN ITS CAPACITY AS DESIGNATED MEMBER OF
SENTINEL HILL NO. 207 LIMITED PARTNERSHIP,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

and

Docket: 2009-2248(IT)G

BETWEEN:

SENTINEL HILL PRODUCTIONS IV CORPORATION,
IN ITS CAPACITY AS DESIGNATED MEMBER OF
SHAAE (2001) MASTER LIMITED PARTNERSHIP,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR ORDERS

Rip C.J.

[1] These are three motions in respect of appeals under the *Income Tax Act* by Robert Strother, Sentinel Hill Productions IV Corporation, in its capacity as designated member of SHAAE (2001) Master Limited Partnership ("SHAAE") and Sentinel Hill Productions IV Corporation, in its capacity as designated member of Sentinel Hill no. 207 Limited Partnership ("Hill No. 207") from determinations of loss issued by the Minister of National Revenue ("Minister") in respect of their 2001 and 2002 taxation years[1]. The motions were heard together.

[2] The appeals relate to investments in film production limited partnerships which were submitted to the Rulings Division of the Canada Revenue Agency ("CRA"). The CRA issued several advance tax rulings which purportedly applied to the particular appellants, partnerships and other interested persons, including the Master Limited Partnerships ("MLPs") and the Production Limited Partnerships ("PLPs"). The appellants state that the CRA decided not to honour these rulings, hence the determinations of loss that do not agree with the losses calculated by the appellants.

[3] Each motion is for:

> 1) An Order pursuant to Rule 53 of the *Tax Court of Canada Rules* (*General Procedure*), ("the *Rules*") striking out all or those portions of the Respondent's Replies, which are enclosed in brackets or, with respect to quotation marks, which are circled[2].

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[1] The Minister assumed the existence of a partnership in making the determinations in the Strother appeal and the SHAAE and the Hill No. 207 appeals. The main difference in these appeals appears to be that in confirming the Strother determination, the Minister denied the existence of a partnership. However, since the appeals of SHAAE and Hill No. 207 were filed 180 days after the determinations and before the determinations were confirmed it is only in the replies that the respondent denied the existence of the partnerships the Minister assumed in making the determinations. Counsel for the appellants suggested that in the SHAAE and the Hill No. 207 appeals the Minister is appealing from his own determinations. This was not argued and is not a matter before me at this time.

[2] 1) To attach as an appendix each of the Replies to the Notices of Appeal would add over 100 pages to these reasons. Therefore I have prepared Appendices A, B, C, D and E to these reasons:

2) An Order pursuant to Rules 147(1), (3)(i) and 5(c) of the *Rules* awarding the Appellant solicitor and client costs with respect to the Motions.

[4] The appellants rely on Rule 53 of the *Tax Court of Canada Rules* (*General Procedure*) ("*Rules*") and complain that numerous portions of the Replies to the Notices of Appeal ("Replies") are scandalous, frivolous and vexatious and an abuse of the Court pursuant to Rule 53[3] in that:

A Re: SHAAE and Hill No. 207 replies:

(a) the bracketed and circled portions do not conform to the specifications of Rule 49(1) of the *Rules*;

(b) the bracketed and circled portion of the Reply are, with respect to the section titled "Overview", advanced as legal arguments and not as statements of fact;

(c) the bracketed and circled portion of the Reply advanced as facts assumed by the Minister in assessing and as further assumptions of fact are conclusions of law and mixed fact and law;

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a) Appendix A sets out the provisions of the reply in the SHAAE appeal that the appellant wants struck. The paragraph numbers and content of this Reply are identical to that that of the Hill No. 207 reply and similar to the Strother reply. (Differences in paragraph numbers are noted in these reasons).

b) In Appendix B, a column entitled "Portions of relevant reply appellant wants struck (bracketed portions of relevant reply)" speaks for itself. Another column informs the reader if the disputed portion is struck or not. Section 1 of Appendix B describes the disputed portions in the SHAAE and Hill No. 207 replies and Section 2 of Appendix B describes those in the Robert Strother reply. The portion of the replies with respect to quotation marks are described in these reasons.

c) Appendices C and D include the Overview and paragraphs 2 to 15 inclusive of the Hill No. 27 and Strother replies, respectively, that are attacked.

2) Note that in the Hill No. 207 and SHAAE motions, the appellants ask that paragraphs 1(i), 1(k), 1(l) and 19 of the replies be struck for more than one reason. Strother asks that paragraphs 1(e), 1(f), 1(g), 20, 26 and 29 be struck for more than one reason.

[3] Although there were concessions offered by the respondent in respect of the Strother appeal, the offer was to change the statement "were not partnerships in law" to "did not carry on business in common with a view to profit" in several paragraphs of the reply. The appellant did not accept the respondent's offer.

(d) the portion of the Reply entitled "Summary of Tax Loss Creation Scheme", paragraphs 2 to 15 inclusive, are neither advanced as facts which the Minister assumed in assessing as in paragraph 46, nor as further assumptions of fact as in paragraph 47. As such, paragraphs 2 to 15 inclusive are simply arguments advanced as fact; and

(e) the bracketed and circled portions of the Reply are argumentative, inflammatory or inserted to colour the proceedings and to usurp the function of the Trial Judge.

B Re: Strother reply:

(a) the bracketed and circled portions do not conform to the specifications of Rule 49(1) of the *Rules*;

(b) the bracketed and circled portions of the Reply are, with respect to the section titled "Overview", advanced as legal arguments and not as statements of facts;

(c) the bracketed and circled portions of the Reply advanced as "Facts" and as "Assumptions of Fact", are conclusions of law or mixed fact and law; and

(d) the bracketed and circled portions of the Reply are argumentative, inflammatory or inserted to colour the proceedings and to usurp the function of the Trial Judge.

[5] The Replies are essentially identical; the majority of the numbered paragraphs referred to above are the same in all three Replies, differences are in footnotes.

"Fresh Step" objection

[6] The respondent has objected to the motion of the appellant Strother on the basis his motion is a fresh step. Rule 8(*b*) provides that:

A motion to attack a proceeding or a step, document or direction in a proceeding for irregularity shall not be made,	La requête qui vise à contester, pour cause d'irrégularité, une instance ou une mesure prise, un document donné ou une directive rendue dans le cadre de celle-ci, ne peut être présentée, sauf avec l'autorisation de la Cour :
…	…
(*b*) if the moving party has taken any	*b*) si l'auteur de la requête a pris une

further step in the proceeding after obtaining knowledge of the irregularity,	autre mesure dans le cadre de l'instance après avoir pris connaissance de l'irrégularité.

except with leave of the Court.

[7] The chronology of events leading to the Strother motion are relevant:

1. January 19, 2007	—	Notice of Appeal for 1998 and 1999 taxation years
2. November 5, 2007	—	Amended Notice of Appeal
3. November 9, 2007	—	Further Amended Notice of Appeal
4. December 18, 2008	—	Another Further Amended Notice of Appeal
5. January 19, 2009	—	Reply to the Further Amended Notice of Appeal dated December 18, 2008.
6. February 13, 2009	—	Appellant's Answer to Respondent's Reply ("The Fresh Step")
7. February 11, 2010	—	Further Further Amended Notice of Appeal
8. February 18, 2010	—	Reply to the Further Further Amended Notice of Appeal dated February 11, 2010.
9. March 26, 2010	—	Appellant filed and served motion to strike.

[8] There are at least two reasons behind the fresh step rule. The first is to prevent prejudice where it is unfair to permit a reversal in approach[4] and the second is based on the idea of an implicit waiver[5]. That is, by proceeding to the next step the party has waived their right to complain of the irregularity. If either underlying factor is not present then there are strong grounds to exercise discretion and grant leave to allow the motion to be heard despite the fresh step.

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4 *Vogo Inc v. Acme Window Hardware Ltd*, 2004 FC 851 at para 60.

5 See also *Imperial Oil Limited and Inco Limited v The Queen*, 2003 TCC 46; *GCC Ltd v Thunder Bay*, (1981), 32 OR (2d) 111 (HC); Garry D. Watson and Lynne Jeffrey, *Holmsted and Watson, Ontario Civil Procedure*, (Carswell), Volume 3 at 2-20.

[9] Both parties rely on Bowman A.C.J.'s (as he then was) statement in *Imperial Oil Limited and Inco Limited v The Queen*:[6]

> The "fresh step" rule is one that has been part of the rules of practice and procedure in Canada and the United Kingdom for many years. There is a great deal of jurisprudence on what constitutes a fresh step but the rule is based on the view that if a party pleads over to a pleading this implies a waiver of an irregularity that might otherwise have been attacked. For two reasons I do not think that the fresh step rule precludes the respondent from bringing the motions. *First, it is clear that by filing replies to the notices of appeal the respondent is not waiving her objections to the filing of the notices of objection and appeal.* The replies clearly state the Crown's objection. *Second, a rather wide ranging attack on the appellant's right to appeal, including allegations that that this court has no jurisdiction, that the appeals are frivolous, vexatious and an abuse of process is hardly an attack on an irregularity.*
>
> [Emphasis added.]

[10] The appellant makes two arguments in respect of why leave should be granted for his motion to strike based on *Imperial Oil*. First the appellant argues that the conclusions of law and repetitive pleadings are beyond a mere irregularity. The facts at bar are not the same as in *Imperial Oil*. There the issue was whether the appellant was entitled to appeal from an initial "quick" assessment, where only the arithmetic was checked, following the expiration of the 90 day period of confirmation. The Crown's argument was that a "quick" assessment did not give rise to a right to object and that it was only after a more thorough assessment that the taxpayer could object. The central issue was whether the Tax Court had jurisdiction to hear an appeal from a "quick" assessment. In that case the fresh step should not prevent the court from making this legal determination.

[11] In this matter, counsel states, the issues in the impugned paragraphs are not determinative of the matter. The criticism that the Reply contains conclusions of law or repetition is more in line with irregularities than determinations regarding the right to appeal. It is not enough that the motion to strike was brought under the heading of frivolous and vexatious proceedings or an abuse of process to fit within Bowman A.C.J.'s statement in *Imperial Oil*. Instead, it must be a substantial attack against the pleading, an attack against the entire appeal itself, and leave should not be granted on this basis.

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6 *Imperial Oil*, supra note 3 at para 20.

[12] The appellant's second argument is that the respondent will not experience any prejudice as the issues are the same in the other appeals proceeding along the same timelines. Additionally, no documents have been exchanged and no discovery has been conducted. The respondent has not indicated how she would be prejudiced in this situation other than to say that the fresh step should be considered if a costs decision in the Strother motion is made. That is, as I understand it, "they shouldn't be able to demand costs in regard to Strother when they have taken actions inconsistent with the present position."

[13] The parties have both filed new pleadings since the fresh step, addressing the issues raised in the Answer. They are effectively still at square one. The respondent and the appellant are in no different position than if the Answer had been the final pleading. Both sides are aware that one of the critical issues in all three appeals is the role of the CRA Rulings and both have given their facts surrounding this issue. Accordingly, in the circumstances, it is not obvious the respondent will suffer any prejudice. Leave for the motion is granted.

The Motions

[14] The requirement as to what a reply in an income tax appeal should state is found in Rule 49(1) of the *Rules*:

Subject to subsection (1.1), every reply shall state	Sous réserve du paragraphe (1.1), la réponse indique :
(*a*) the facts that are admitted,	*a*) les faits admis;
(*b*) the facts that are denied,	*b*) les faits niés;
(*c*) the facts of which the respondent has no knowledge and puts in issue,	*c*) les faits que l'intimée ne connaît pas et qu'elle n'admet pas;
(*d*) the findings or assumptions of fact made by the Minister when making the assessment,	*d*) les conclusions ou les hypothèses de fait sur lesquelles le ministre s'est fondé en établissant sa cotisation;
(*e*) any other material fact,	*e*) tout autre fait pertinent;
(*f*) the issues to be decided,	*f*) les points en litige;
(*g*) the statutory provisions relied on,	*g*) les dispositions législatives invoquées;
(*h*) the reasons the respondent intends to rely on, and	*h*) les moyens sur lesquels l'intimée entend se fonder;
(*i*) the relief sought.	*i*) les conclusions recherchées.

[15] Once the respondent has admitted and denied facts and stated she has no knowledge of certain facts alleged in the Notice of Appeal and puts these facts in

issue, there are only two more statement of facts for the respondent to plead: the finding or assumptions of fact made by the Minister when making the assessment, and any other material fact. All these statements of fact are to be statements of material fact, not immaterial facts, not statements or principles of law and not statements mixing fact with law. Subparagraphs *f*), *g*) and *h*) of Rule 49 accord the respondent opportunity to describe the issues, state the statutory provisions in play and submit the reasons she is relying on in this appeal.

[16] It is poor and improper pleading when a litigant admits or denies a fact in a pleading but couples the admission or denial with a conclusion of law or some extraneous comments that add nothing to the process. The assumptions of fact should be facts the Minister relied on in assessing and the facts so relied on should be material facts. Otherwise, why were these facts relied on if they were not material? In *Foss v. The Queen*[7] my colleague Bowie J. explained that:

> The purpose of pleadings is to define the issues between the parties for the purposes of discovery, both documentary and testamentary, and trial. That requires no more than a statement of the "precise findings of fact" that underpin the assessment. It is potentially prejudicial to the appellant to plead more - certainly to plead more by way of assumptions of fact. The appellant is, of course, entitled to particulars of the evidence that the Crown intends to lead at trial, but these are properly obtained on discovery, not disguised as material facts as to which the Crown at trial may claim a presumption of truth. …

I Mixed fact and law

[17] The appellants submit that the ratio of Rothstein J.A. (as he then was) in *The Queen v. Anchor Pointe Energy Ltd.*[8] regarding conclusions of mixed fact and law should be extended to all paragraphs of the Reply which deal with facts:

> [25] I agree that legal statements or conclusions have no place in the recitation of the Minister's factual assumptions. The implication is that the taxpayer has the onus of demolishing the legal statement or conclusion and, of course, that is not correct. The legal test to be applied is not subject to proof by the parties as if it was a fact. The parties are to make their arguments as to the legal test, but it is the Court that has the ultimate obligation of ruling on questions of law.
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> [26] However, the assumption in paragraph 10(z) can be more correctly described as a conclusion of mixed fact and law. A conclusion that seismic data

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7 2007 TCC 201, [2007] T.C.J. No. 99 (QL).

8 2003 FCA 294, at paras 25-26.

> purchased does not qualify as CEE within the meaning of paragraph 66.1(6)(*a*) involves the application of the law to the facts. Paragraph 66.1(6)(*a*) sets out the test to be met for a CEE deduction. Whether the purchase of the seismic data in this case meets that test involves determining whether or not the facts meet the test. The Minister may assume the factual components that are being assumed so that the taxpayer is told exactly what factual assumptions it must demolish in order to succeed. It is unsatisfactory that the assumed facts be buried in the conclusion of mixed fact and law.

[18] In *Anchor Pointe* the Court opined that the assumptions of fact be factually clear and the Crown should not draft the assumptions of fact in such a way as to exacerbate the appellant's onus of disproving the facts assumed. The appellant does not require this protection in portions of the Reply where the Crown has the onus of proof, for example, paragraphs *a*), *b*), *c*) and *e*) of Rule 49(1).

[19] The form of the Reply set out in Rule 49(1) contemplates the avoidance of commingling facts with law. Facts are required to be plead first through paragraphs 49(1)(*a*)(*b*)(*c*) and (*e*). Rule 49(1)(*d*) restricts the respondent to pleading findings of fact or assumptions of fact made by the Minister in assessing; there are material facts only. Rules 49(1)(*f*) to (*i*) inclusive give the respondent the right to plead matters described in these Rules. This is similar to the rules of practice in common law provinces, including Ontario and British Columbia as well as the Federal Court which allow the pleading of law if the factual underpinnings have been pled[9].

[20] The respondent argues that Rule 49 merely sets out what must be included and does not establish a specific structure. In other words, so long as the requirements of Rule 49 are met, it is possible to intersperse conclusions of law with the facts throughout. To accept the respondent's argument would lead to incoherent, repetitious pleadings as difficult and frustrating as the ones faced with under this motion.

[21] It does not require complex statutory analysis to arrive at the conclusion that a "fact" means a fact in the legal context. The majority of the Supreme Court of Canada took a technical interpretation approach to the word "sale" in the *Income Tax Act* with Major J. stating: [10]

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[9] *Rules of Civil Procedure*, RRO 1990, Reg 194, r 25.06(2); *Supreme Court Civil Rules*, BC Reg 168/2009, r 3-7(9); *Federal Court Rules*, SOR/98-106, r 175.

[10] *Will-Kare Paving & Contracting Ltd v. The Queen*, 2000 SCC 36 at para 31, [2000] 1 SCR 915.

> To apply a “plain meaning” interpretation of the concept of a sale in the case at bar would assume that the *Act* operates in a vacuum, oblivious to the legal characterization of the broader commercial relationships it affects. It is not a commercial code in addition to a taxation statute. Previous jurisprudence of this Court has assumed that reference must be given to the broader commercial law to give meaning to words that, outside of the *Act*, are well-defined. …

[22] In terms of "facts", this word is in the rules of civil procedure and so should be interpreted in the legal context with the relevant distinctions between questions of law, questions of fact and questions of mixed fact and law. The word "facts" excludes conclusions of law and mixed fact and law.

[23] The appellants claim that the disputed bracketed portions of the Replies are actually conclusions of law or mixed fact and law. However, the respondent states that these are simply factual assertions.

[24] It is frequently difficult to draw the line between a question of fact and a question of law. It is more difficult when the third category, mixed question of fact and law, is considered. Iacobucci J. of the Supreme Court of Canada recognized this problem and stated the following: [11]

> … Briefly stated, questions of law are questions about what the correct legal test is; questions of fact are questions about what actually took place between the parties; and questions of mixed law and fact are questions about whether the facts satisfy the legal tests. A simple example will illustrate these concepts. In the law of tort, the question what "negligence" means is a question of law. The question whether the defendant did this or that is a question of fact. And, once it has been decided that the applicable standard is one of negligence, the question whether the defendant satisfied the appropriate standard of care is a question of mixed law and fact. I recognize, however, that the distinction between law on the one hand and mixed law and fact on the other is difficult. On occasion, what appears to be mixed law and fact turns out to be law, or *vice versa*.

a) Arm’s length relationship

[25] The following portions of these reasons deal with various words, terms and phrases that the appellants view as conclusions of law or mixed fact and law. In an effort to make the reading of these reasons less onerous to the reader, I shall refer to the portions of the SHAAE Reply which have been bracketed or circled by the

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[11] *Canada (Director of Investigation and Research) v Southam Inc.*, [1997] 1 SCR 748 at para 35.

appellants as well as the portion of the Reply in SHAAE that is entitled "Summary of Tax Loss Creation Scheme", rather than to the same matters in the Strother and Hill No. 207 appeals.

[26] A non-arm's relationship is a question of fact: *Teelucksingh v The Queen*[12]. Bowie J. explained that matters such as:

> … assertions as to value, *that parties do not act at arm's length*, that they did not carry on a business, that expenses were not incurred, or were not incurred for a particular purpose *are assertions of fact*. Certainly those facts have legal implications, and some of them use words that are used in the *Act*, but they are nevertheless factual assumptions.
>
> [Emphasis added.]

[27] Accordingly, any mention of non-arm's length relationship cannot be struck on the basis of pleading a conclusion of law. Alternatively, in some cases they can be struck on the basis of being inappropriate for a definition which is discussed below.

Bracketed portions **not struck** from the Strother appeal:

Paragraphs 24 and 46(llll) – Title, 46(pppp) – Title, as the statements of a non-arm's length relationship are not conclusions of law.

b) Did not carry on business with a common view to profit

[28] The Supreme Court of Canada stated the test for partnership as follows: [13]

> … In other words, to ascertain the existence of a partnership the courts must *inquire into whether the objective, documentary evidence and surrounding facts, including what the parties actually did, are consistent with a subjective intention to carry on business in common with a view to profit.*
>
> Courts must be pragmatic in their approach to the three essential ingredients of partnership. Whether a partnership has been established in a particular case will depend on an analysis and weighing of the relevant factors in the context of all the surrounding circumstances. That the alleged partnership must be considered in the

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12 2010 TCC 94, at para 11; see also *Cameco Corporation v. The Queen*, 2010 TCC 636, at para 40-41.

13 *Backman v. The Queen*, 2001 SCC 12 at para 25-26, [2001] 1 SCR 367.

> totality of the circumstances prevents the mechanical application of a checklist or a test with more precisely defined parameters.
>
> [Emphasis added.]

[29] Based on Iacobucci J.'s reasoning in *Southam*, the test for a partnership would be a conclusion of mixed fact and law. What the PLPs and MLPs did or did not do are questions of fact; what is the test for partnership is a question of law and whether the facts allow the appellants to satisfy the *Backman* test would be a mixed question of fact and law.

[30] The respondent therefore is required to extricate the legal components of a conclusion of mixed fact and law and only plead the facts where the rule requires facts. The statement that "… did not carry on business with a view to profit" will be struck when commingled with the facts:

> The paragraphs struck from the SHAAE and Hill No. 207 appeals:
>
> Paragraphs 1(i), (k), (l), 18, 19, 20, 21, 24[14] and 46(f).
>
> Bracketed portions struck from the Strother appeal:
>
> Paragraphs 1(e), (f), (g), 18, 20, 29 and 46(h).

c) The allegations of sham, circular transactions or façade

[31] The allegations of sham, circular transactions and facades are also in issue. The test for the sham doctrine was set forth in *Snook v. London West Riding Investments, Ltd.*:[15]

> … [Sham] means acts done or documents executed by the parties to the "sham" which are intended by them, to give to third parties or the Court, the appearance of creating between the parties, legal rights and obligations different from the actual legal rights and obligations (if any), which the parties intend to create. … for acts or documents to be a "sham", with whatever legal consequences follow from this, *all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating*. …

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14 Paragraph 24 of the SHAAE appeal and paragraph 25 of Hill No. 207 appeal.

15 [1967] 1 All ER 518 at 529.

[Emphasis added.]

[32] In this case, the facts are the actual rights and responsibilities as well as what the parties did or did not do. However, applying the facts to determine whether there was a common intention to mislead is a conclusion of mixed fact and law as it involves the applications of the facts to the legal test of sham. Again, the respondent is required to extricate the facts and mentions of sham, or façade should be deleted. With respect to this argument, some of the bracketed portions are struck while some are not as they are factual underpinnings and not conclusions.

> Bracketed portions struck from the SHAAE and Hill No. 207 appeals.
>
> Paragraphs 19, 22, 24[16] and 46(c).
>
> Bracketed portions struck from the Strother appeal:
>
> Paragraphs 20, 22, 26, 29, 46(c) and (q).
>
> Bracketed portions **not struck** from the SHAAE and Hill No. 207 appeals:
>
> Paragraphs 46(a), (b) and (ss) are not struck as they are the factual underpinnings of a sham argument.
>
> Bracketed portions **not struck** from the Strother appeal:
>
> Paragraphs 27, 46(a), (b), (o), (dd), (oo), (nnn), (pppp) and (tttt) are not conclusions of law but factual underpinnings sham.

[33] The difficult term here is "circular" and its derivatives. The appellant's main complaint with "circular" is that it is colourable and only in oral submissions did appellants' counsel mention that it could be a legal conclusion. However, "circular" is a factual conclusion; it is a factual description. Therefore, no portions containing this word will be struck on this basis alone. The colourability of these terms, though, will be discussed below.

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[16] Paragraph 24 of SHAAE appeal and paragraph 25 of Hill No. 207 appeal.

d) Reasonable expectation of profit ("REOP")

[34] The Supreme Court of Canada replaced the REOP test for deductibility under section 9 with the pursuit of profit test in *Stewart v. The Queen*[17]. It is now a two part test:

> (i) Is the activity of the taxpayer undertaken in pursuit of profit, or is it a personal endeavour?
>
> (ii) If it is not a personal endeavour, is the source of the income a business or property?

[35] The Supreme Court of Canada went on to say that "[the] overall assessment to be made is whether or not the taxpayer is carrying on the activity in a commercial manner" with a reasonable expectation of profit being a factor to consider[18].

[36] Therefore, the REOP test is still a relevant factor to consider when determining whether the activity was carried on in a commercial manner or alternatively for determining whether a partnership existed. For example, in *Foster v. The Queen*,[19] Angers J. cited no income as one factor in concluding that the partnership was not a partnership in law in the context of SR&ED tax shelter program.

[37] Therefore, reference to REOP is not a conclusion of law and but a fact relied upon by the Minister and as a result its mention should not be struck.

> Bracketed portions **not struck** from the SHAAE and Hill No. 207 appeals:
>
> Paragraph 46(aaa).
>
> Bracketed portions **not struck** from the Strother appeal:
>
> Paragraph 37.

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17 2002 SCC 46 at para 50, [2002] 2 SCR 645.

18 *Ibid*, at para 55.

19 2007 TCC 659 at para 34, 2008 DTC 2450, [2008] 4 CTC 2242.

e) Response to rulings allegations

[38] Paragraphs 28 through 34 of the SHAAE appeal and paragraphs 30 through 36 of the Strother appeal are the respondent's response to the appellant's allegation that it had received a favourable ruling in respect of the tax shelter arrangement. The only conclusion of law in these paragraphs is in paragraph 34 of the SHAAE and paragraph 35 of the Hill No. 207 appeals which state that the appellants do not qualify for the equitable defense of estoppel.

> Bracketed portions struck from the SHAAE and Hill No. 207 appeals
>
> Only a portion (the last sentence) of each of paragraph 34 and paragraph 35 is struck from the SHAAE and Hill No. 207 appeals respectively for this reason.

II Should portions of the replies be struck for being repetitive or redundant?

[39] The appellants' alternative argument to strike is based on the repetition and redundancy of the Replies. When reading through redundant and repetitive portions of the Replies it is only a matter of pages before one has the feeling that one of the parties is trying to beat the other into submission, never mind the judge who is only just entering the fray. The appellants rely on *Mudrick v Mississauga Oakville Veterinary Emergency Professional Corporation*[20], in which Master Haberman of the Ontario Superior Court of Justice struck out the plaintiff's overview and summary for this very reason. In reaching this conclusion Master Haberman stated:[21]

> The pleading contains a summary, which essentially repeats the overview. This will be unnecessary when the claim is pleaded properly. Including the summary and the overview means the same things are repeated three times in the pleading. They should only be discussed once, in the body of the claim, where they fall chronologically.

In concluding, he added the following general comments regarding pleadings in general: [22]

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20 [2008] O.J. No. 4512 (QL).

21 *Ibid*, *Mudrick* at para 31.

22 *Ibid, Mudrick*, at para 40.

> Repetition should be avoided. Superfluous detail should be eliminated. Editorialized comments should be removed. … This is not "the last chance" to tell the whole story – it is only an overview of what the case will be about. …

[40] Moreover, Bowie J. cited the following passage from *Holmsted and Watson* regarding the rule of pleading: [23]

> This is *the* rule of pleading: all of the other pleading rules are essentially corollaries or qualifications to this basic rule that the pleader must state the material facts relied upon for his or her claim or defence. The rule involves four separate elements: (1) every pleading must state facts, not mere conclusions of law; (2) it must state material facts and not include facts which are immaterial; (3) it must state facts and not the evidence by which they are to be proved; (4) it must state facts concisely in a summary form.

The fourth requirement is particularly relevant to this appeal. A repetitive pleading is not concise. It does nothing to help in understanding the issues.

[41] Orsborn J. (as he then was) of the Newfoundland and Labrador Supreme Court, when faced with repetitive pleadings, explained: [24]

> … The pleadings define the case to be made out and to be met, both factually and legally. Loosely defined and unfocussed pleadings are of no benefit to the recipient or to the court. They detract from rather than facilitate the understanding of the legal framework against which the factual circumstances will be assessed. *Unnecessarily verbose and repetitive pleadings create uncertainty*; there is no place for uncertainty when faced with responding to a claim for redress.
>
> [Emphasis added.]

[42] Finally, P.M. Perell J. of the Ontario Superior Court of Justice cited repetition as one of his reasons for striking certain paragraphs of a statement of claim under Rule 25.11 of the Ontario *Rules of Civil Procedure*[25].

> I strike out these paragraphs or words on the grounds that they are *any or all* of immaterial, embarrassing, argumentative, tautological, *redundant, repetitious*, or a pleading of evidence and not a material fact. …[26]

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23 *Foss*, supra note 6 at para 6; see also *Globtek Inc v. The Queen*, 2005 TCC 727 at para 5 and 13.

24 *Duffett v. Canada (AG)* 2004 NLSCTD 58 at para 23, 235 Nfld & P.E.I.R. 321.

25 This rule identical to Rule 53.

26 *Robinson v. Medtronic Inc*, 2010 ONSC 1739 at para 19.

[Emphasis added.]

[43] The excessive repetition within each Reply is superfluous and undermines the goals of conciseness and certainty. The repetitive portions should be struck.

a) Redundancy of Overview and Summary

[44] The most redundant portions of the Replies are the Overview and the Summary which effectively repeat the allegations made in paragraphs 46 and 47. In *Gould v The Queen*[27], Bowman J. refused to strike an overview which described the overall "scheme". To Bowman J. it was a relevant fact that charitable donations were part of a larger pattern involving others. Finally, he allowed it to remain as it served a function of pleadings; to inform the judge of the Crown's position as well as the issues he must decide upon[28]. An overview can be a welcome addition in pleadings, in particular pleadings in a complex matter. It gives the reader a bird's eye view of the issue. It can be analogous to an Executive Summary of a lengthy report so long as it is used as such. That it may be colourful — as long as it is not overtly one-sided — should not unduly concern the opposing party in an appeal before this Court. There is no jury. The judge can readily discern fact from hyperbole. Ideally, however, the overview should present a fair description of the issue in appeal. Inflammatory language in an overview serves mainly to make the litigation less civil. The overviews in these Replies are allowed to remain. Like in *Gould*, these appeals also are concerned with a tax shelter program.

[45] The same cannot be said for each Summary. Each repeats the Overview as well as paragraphs 46 and 47 of the Replies. The respondent should choose one or the other. The reader has already been put on alert as to the central issues in the appeal as well as the Crown's position. It is redundant and must be struck in all three appeals as scandalous, frivolous and vexatious.

The paragraphs struck in the SHAAE and Hill No. 207 Appeals.

Paragraphs 2-15(Summary), 19, 20, 23, 24[29].

Bracketed portions struck from the Strother appeal

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27 2005 TCC 556, 2005 DTC 1311.

28 *Ibid*, at para 11-12.

29 Paragraph 24 in SHAAE appeal and paragraph 25 of Hill No. 207 appeal.

Paragraphs 2 through 15 (Summary), 20, 22, 26 and 29.

III Should portions of the Replies be struck for use of colourable or embellishing language?

[46] With respect to terms used for colour or to embellish, the respondent submitted *Meditrust Healthcare Inc v. Shoppers Drug Mart* as authority for what is colourable language. There Molloy J. stated: [30]

> … Strong language is not prohibited when appropriate to the context. … That said, distinguishing between particular words or expressions which are merely descriptive, as opposed to inflammatory, is largely a subjective exercise. My own view is that considerable latitude should be given to the style and language chosen by counsel. The Court should only intervene when the expressions used are clearly "over the line".

[47] Justice Molloy then ruled that the following statements did not cross the line: "fraudulent intent", "bogus letter", "warning", "threatened", "vested interest in maintaining dominance", "propagandizing directly and through surreptitious means", "pervert", "predatory practice", "poisoning the marketplace", "poisoning the business of the plaintiff", "modus operandi", and "agent provocateur in the context of an action for anti-competitive practices". On the other hand he struck the expression "dirty tricks" as inflammatory[31].

[48] The appellant cited *George v. Harris*,[32] for the position that "… portions of a pleading that are irrelevant, argumentative or inserted for colour, or that constitute bare allegations should be struck out as scandalous". However, *George v. Harris* dealt with paragraphs of a notice of motion relating to deficiencies in an affidavit of documents. As such, most of the words related to the conduct of the defendant in failing to comply with discovery. The following are examples of words struck: "deliberately avoids disclosing", "used concealment techniques", "manipulated form and content of affidavit", "deliberateness of documentary disclosure evasions", "evasions" and "deliberate gaps".

[49] The issue here is whether the word "circular" and its derivatives are over the line. This is a subjective determination. In this case, the references to circular transactions do not come close to the offensive terms in *Meditrust* or *George v.*

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30 85 ACWS (3d) 761, 1999 CarswellOnt 5285 at para 33

31 *Ibid*, at para 34.

32 [2000] O.J. No. 1762 (QL), at para 20.

Harris. They are relevant in the context of a tax shelter arrangement and nothing is scandalous if it is relevant[33]. As a result no paragraphs are struck based on colourability.

> Bracketed portions **not struck** from the SHAAE and Hill No. 207 appeals:
>
> Paragraphs 46(j), (p), (q), Page 20 Title and Page 20 Subheading I, 47(f), (g), (kk), (pp) and (pp)(iv).
>
> Bracketed portions **not struck** from the Strother appeal:
>
> Paragraphs 39, 46(l), (p), (r), (s), (t) (v), (v), (zz), (ggg), (hhh), (zzz), (aaaa), (eeee), (ffff)(f), (llll) – Title.

IV Should the qualifications to the definitions be struck?

[50] The respondent has qualified the definitions portion of its Replies to the point where the definitions are useless. This practice should be discouraged. It is no use having a definition unless the opposing party and the trial judge can easily refer to the definition as well. The practice prevents the other party from relying upon a standard term when the qualification is in dispute. Moreover, it prevents the judge from using the standard term before the finding of fact is made as to the qualification. Definitions are not an explicit requirement under Rule 49; they are permitted because they simplify the pleadings. Where the definition introduces a lack of clarity through qualifications, the ability to include definitions should be curtailed. For example, in *Sun Life Assurance Co. of Canada v. 401700 Ontario Ltd*, the Ontario Court (General Division) held that: [34]

> … defined terms and descriptive phrases in a pleading are generally within the discretion of the party pleading. They are often of assistance to the smooth flow of the pleading. However, defined terms in a pleading should not be inflammatory, nor create an unnecessarily repetitive and prejudicial flavour.

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33 *Quizno's Canada Restaurant Corp. v Kileel Developments Ltd*, (2008) 92 O.R. (3d) 347 (CA); *Ontario (A.G.) v Dieleman* (1993), 14 OR (3d) 697 (Gen Div); *Erinco Homes Ltd*, (*Re*) [1977] O.J. No. 1415 (QL) (Ont HC).

34 (1991) 3 O.R. (3d) 684 at 687.

[51] The qualifications here are certainly repetitive and done to be inflammatory. These qualifications only decrease the clarity of pleading. This is not to say that the particular qualifications have no place in the pleadings, simply that they should be pled separately from the definitions. As a result, all qualifications are struck.

> Bracketed portions of the paragraphs to be struck in the SHAAE and Hill No. 207 appeals:
>
> Paragraphs 1(i), (k), (l), (o), (r), (s) and (t).
>
> Bracketed portions of the paragraphs to be struck from the Strother appeal:
>
> Paragraphs 1(e), (f), (g), (k), (n), (p)

V Miscellaneous portions in Strother

[52] Paragraph 50(iii) is not an allegation of law but merely a purported explanation of the Minister's assessment position. It is a self-serving, useless inclusion in the reply that adds absolutely nothing to the issues to be decided.

[53] Footnote to paragraph 43 is not struck as there is nothing offensive with what is contained therein but I question if it is necessary to name these appellants in the pleadings.

VI Respondent's agreement to delete quotation marks

[54] At trial respondent's counsel agreed to remove the disputed quotation marks throughout the Reply and instead place the word "purported" in their place. Therefore the following portions of the paragraphs are struck with leave to amend:

> Bracketed portions struck from the SHAAE and Hill No. 207 appeals:
>
> Quotation marks contained in the Overview, paragraphs 22, 36, 41, 46(g), (j), (m), (n), (vv) and (bbb).
>
> Bracketed portions struck from the Strother appeal:

Quotation marks in paragraphs 38, 39, 40, 41, 42, 46(l), (o), (p), (s), (t)(i), (t)(ii), (t)(iii), 46(jj), 46(qq), 46(vv), 46(ggg) – Title[35], 46(iii), 46(nnn), 46(qqq), 46(ssss), 46(uuuu), 46(zzzz), 46(ccccc) and 48.

Conclusion

[55] Orders in each motion shall be issued accordingly. The respondent shall have until June 30, 2011 to amend the portions of the Replies struck and serve and file its Amended Replies. The appellants shall have 30 days thereafter to serve and file Answers to the Replies.

[56] One set of costs shall be awarded to the appellants. The appellants asked for costs on a solicitor-client basis and I invite counsel to make submissions in writing if they cannot agree on a fixed amount by June 30, 2011.

Signed at Ottawa, Canada, this 12th day of May, 2011.

"Gerald J. Rip"

Rip C.J.

[35] Not circled by Appellant but I suspect this is oversight.

Appendix B – Chart of Disputed Statements and Paragraphs

Section 1

Section 2

The Robert Strother Appeal 2007-329(IT)G

Paragraph	**Portions of Relevant Reply Appellant Wants Struck (Bracketed Portions of Relevant Reply)** (Where [] used, only portion contained in [] is in dispute)	**Strike?**	
Overview	Entirety reproduced in Appendix D for Robert D. Strother	No	
1(e)	Was not a partnership in law		Yes
1(f)	…were not partnerships in law;		Yes
1(g)	…though was not a partner in law		Yes
1(k)	…and each is a corporation which did not operate at arm's length with the Studios;		Yes
1(n)	…which acted as a conduit for the circulation of funds, and did not operate at arm's length with the Investors, the Sentinel Group, the MLP or any of the PLPs;		Yes
1(p)	"Emeritus Trust" …which acted as a conduit for the circulation of funds, and did not operate at arm's length with the Investors, the Sentinel Group, the MLP or any of the PLPs;		Yes.
2 – 15	"Summary of Tax Loss Creation Scheme" reproduced in Appendix D for Robert D. Strother.		Yes
18	…since each lacked the essential ingredient of carrying on business in common with a view to profit…		Yes
20	…He states that neither the MLP nor any of the PLPs was a partnership in law since each lacked the essential ingredient of carrying on business in common with a view to profit. He states further that the MLP and PLPs were each exclusively formed for the purpose of entering into a series of circular transactions designed to create tax losses for the Investors and to siphon off the only cash into the hands of the promoters and Studios. He states further that some or all of the "transactions" were designed to create a façade, one that differed greatly from reality.		Yes

22	…He states further that that the circular character of the underlying "transactions" insured the investors would be exposed only to the extent of their cash contribution. He states further the transactions were *designed* to eliminate any prospect of profit by the Investors except insofar as they might be able to acquire tax losses.		Yes
24	…If in fact the Lender did make such loans, the Lender was not acting at arm's length with the MLP	No	
26	…He states further that the alleged contracts were sham transactions, incomplete and/or legally ineffective. He specifically denies that the PLPs provided any services whatsoever under "contracts". He states further that the Net Profit Participation clauses were each structured and intended to be worthless and were, in fact, worthless		Yes
27	…He states further that the purported options were not genuine options. Rather, to fulfill the real agreement of renting their expenses, the Studios treated the "options" as if they were mandatory. The "options", when exercised, would be set off against and eliminate any liability on the part of the Investors in excess of their cash contributions. He specifically denies that the option price for the Class B units was set at a fair market value and states further that the fair market value of the Class B units was nil.	No	
29	…since each lacked the essential ingredient of carrying on business in common with a view to profit. He states further that the MLP and PLPs were each exclusively formed for the purpose of entering into a series of circular transactions designed to create tax losses for the Investors and to siphon off the only cash into the hands of the promoters and Studios. He states further that some or all of the "transactions" were designed to create a façade, one		Yes

	that differed greatly from reality.		
30	…He states further that an advance tax ruling respecting the transaction described in the Further Amended Notice of Appeal was neither sought by anyone nor given by Canada Revenue Agency ("CRA"). He states further that the CRA had no correspondence or discussions in respect to the transactions described in the Further Amended Notice of Appeal upon which the appellant, the Sentinel Group, the Investors or the MLP might rely.	No	
31	…He states further that the taxpayers seeking the October 6, 1998 ruling did not disclose all of the relevant facts. Had the taxpayers seeking the October 6, 1998 ruling fully and accurately disclosed the relevant facts, the Rulings Directorate may have either refused to rule on the transactions or may have provided an unfavourable ruling. He otherwise denies the allegations of fact set out in those paragraphs.	No	
32	He states further that the appellant, the Sentinel Group, the Investors or the MLP knew or ought to have known that no advance tax ruling was ever sought by anyone or given by the CRA with respect to the transactions described in the Further Amended Notice of Appeal. He states that the appellant, the MLP, PLPs and the Investors knew or ought to have known that the ruling related to different transactions and difference taxpayers, was obtained without full disclosure of all of the relevant facts and that the transactions described in the Further Amended Notice of Appeal, in any event, would not satisfy the various caveats and limitations contained within the ruling.	No	
33	…and states further that the statement of facts given to Rulings by the appellant was found by the auditor to be materially different than the transactions in issue.	No	

34	…He states further that the ruling related to different transactions and different taxpayers, was obtained without full disclosure of all of the relevant facts and that the transactions described in the Further Amended Notice of Appeal in any event would not satisfy the various caveats and limitations contained within the ruling.	No	
35	He states that the reassessments regarding the appellant's and the Investors' 1998 and 1999 taxation years were not issued in contravention of any ruling. Advance income tax ruling apply only to the transactions specified in the ruling. No ruling was obtained in respect of the transactions at issue.	No	
36	In any event, the reassessments are consistent with the Minister's interpretation of the law contained in the October 1998 ruling.	No	
37	…at a time when each of the PLPs was in a loss position and each had no reasonable expectation of profit or of even recovering its loss.	No	
39	…so-called…	No	
43 – Footnote 2	With respect to the inducement payment of $571,026 paid by the MLP to some of the Investor's [*sic*], some appellant's [*sic*] were allocated the income inclusion, but were not reassessed by the Minister. The appellants include Gus Baril ($24,000) Leslie Baril ($24,000); Malcolm MacLean ($5,559); Magic Bullet Enterprise Limited ($125,000) and Parian Holding Limited ($5,000)	No	
46 (a),(b) & (c)	The Real Arrangement (a) the Sentinel Group sought to purchase the NCLEs of the Studios. The Studios agreed to receive a fee equal to a negotiated percentage of the Films' budget for renting its production expenses to the Investors indirectly through the PLPs and the MLP;	(a) and (b) are not struck	(c) is struck

	(b) the purchase and sale of PLP Production expenses was the real arrangement between the Studios and the Sentinel Group; (c) to carry out the tax loss creation scheme, the Sentinel Group, the Studios, the MLP, the PLPs and other accommodators entered into a series of "transactions" that did not reflect the true relationship of the parties;		
46 (h)	The MLP and the members of the MLP did not carry on business in common with a view to profit		Yes
46(l)	…at best "window dressing"…	No	
46 (o)	The MLP never intended to profit from its "investment" in the PLPs but rather the MLP's sole intention was to acquire the losses resulting from the tax loss creation scheme;	No	
46(p) – Title	…circular and	No	
46(p) Sub-heading	Circularity of…	No	
46(q)	The Studios and the Sentinel Group created a series of "contracts" and "agreements" which did not reflect the true relationship between the parties;		Yes
46(r)	The "contractual" obligation to provide the NCLE production services was circular;	No	
46(s)	…back the obligation…	No	
46(t)(v)	…thus completing the circle of contractual obligation to provide NCLE production services;	No	
46(v)	…conjured up…	No	
46(dd)	It is widely understood among participants in the movie and television industries that net profit participants rarely, if ever, earn any amounts from their net profit participations;	No	
46(oo)	The MLP and the Sentinel Group marketed nothing more than a	No	

	scheme to access the expenses of the Studios through the PLPs, not a genuine investment in the movie or television industries.		
46(zz)	…the very same NCLE…that the PLPs had contracted to provide to the THC under the NCLE Agreements;	No	
46(ggg)	The financing of the Investors' non-cash investment in the MLP and the financing of the NCLE production services were both circular and accomplished by a series of pre-ordained set-off transactions;	No	
46(hhh)	The series of set-off transactions did not add any additional cash beyond the Investor cash contribution of $288.36 per unit. Rather, the circularization of "funding" and the extinguishment of loans was simply achieved through a series of Directions to Pay and Acknowledgements of Receipt;	No	
46(nnn)	$127,374,310 is "borrowed" by the PLPs [indirectly] from [the Studios through] the THC on a non-interest bearing basis…	No	
46(zzz) – title	All outstanding debt obligations settled by set off	No	
46(aaaa)	The outstanding debt obligations and the corresponding interest obligations of the Emeritus Trust, the Veritus Trust and the Investors are all settled by circular set-offs;	No	
46(eeee)	…thus completing the circle[6] All of the "payments" in the circle described were accomplished by a mere direction to pay. Neither the Veritus Trust nor the Emeritus Trust had the ability to make the annual payment in respect of their respective interest obligations. Neither Trust even maintained a bank account from which payment might be made.	No	
46(ffff)(f)	…thereby completing the circle;	No	
46(llll) – title	Subsection 96(2.2)(c) – [non-arm's length loan and circular loan transactions]	No	

46(pppp)	…that, through its trustee, the Veritus Capital Corp. ("VCC"), acted as a conduit for the circulation of funds.	No	
46(pppp) – title	Non-Arm's Length Investor Loans	No	
46(tttt)	The Sentinel Group carried on the stated business activities of the Veritus Trust;	No	
50(iii)	The entire loss claimed by the MLP ought to have been disallowed but, in light of subsection 152(1.4) of the *Act*, the loss determined was not reduced by the confirmation;		Yes

Appendix D

Overview and Paragraphs 2-15 ("Summary of Tax Loss Creation Scheme") in the Reply for **Robert C. Strother**

Overview

U.S. Major Motion Picture Studios incurred production expenditures in carrying on the business of making movies. Canadian tax shelter promoters rented these expenditures. But, the rental of expenditures does not give rise to a cognizable deduction or loss in Canada.

The Studios and Canadian promoters or their respective designates purported to enter into a series of intricate, circular transactions designed to permit the promoters and their clients to indirectly do what they could not do directly. However, the Studios and the promoters did not deal with the "transactions" as if they were genuine and simply ignored the supposed rights and obligations, when and as required to carry out their real intentions. The "transactions" were designed to create a facade of reality quite different from the disguised reality. The true nature of the relationship between the Studios and the promoters was simply this: the Studios rented to the promoters a portion of the Studios' expenditures.

Neither the Sentinel Hill 1998 Master Limited Partnership (the "MLP") nor any of the three Production Limited Partnerships (the "PLPs") in which the former "invested" were partnerships in law. While fashioned to have the appearance of possessing the legal attributes of a partnership, the MLP and the PLPs lacked the essential ingredient of carrying on business in common with a view to profit. On the contrary, the *sole* purpose of the MLP and the PLPs was to create tax losses for use by the members.

In addition, in the 1999 taxation year, the appellant received an inducement payment in respect of his acquisition of units in the MLP. The appellant incorrectly characterizes the payment as a rebate and a capital receipt.

On objection, the Minister concluded that his reassessment of the appellant's 1998 and 1999 taxation years had been *too generous* as the MLP and PLPs had never been partnerships and thus the appellant should have been permitted *no* losses. In his confirmation, the Minister did not reduce the appellant's losses but merely confirmed that the losses, if any, did not exceed the losses reassessed.

If the transactions were genuine and the MLP and PLPs were in fact partnerships at law, the Minister nevertheless correctly concluded that the appellant had failed to demonstrate the losses incurred, if any, exceeded amounts allowed by the reassessment or were reasonable in the circumstances.

Summary of Tax Loss Creation Scheme

2. The Studios incurred expenditures in the production of motion pictures. For a fee, the Studios agreed to rent a portion of their production expenditures to Canadian promoters who marketed them in Canada as deductible expenses through tax shelters.

3. The promoters and the Studios purported to enter into a series of intricate, circular transactions (collectively referred to as "tax loss creation scheme") designed to enable the promoters and their clients to do indirectly what they could not do directly: to deduct losses derived from a simple rental of expenditures. Some or all of the transactions comprising this tax loss creation scheme were sham transactions, incomplete, and/or legally ineffective. For example, by the time the production services contracts were executed, the Studios had already incurred part or all of the very expenditures and provided part or all of the very services that the PLPs contracted to provide. In some cases, the production services were already entirely completed.

4. To carry out the tax loss creation scheme, the promoters created the MLP, whose purpose was to acquire Class A units of the PLPs. The PLPs contracted to provide production services respecting motion pictures.

5. The Studios contracted with THCs to produce motion pictures. The THCs then contracted with the PLPs to provide production services. The PLPs contracted back with the Studios and the Studios provided the services at cost plus a mark-up.

6. To create the tax losses, each of the PLPs agreed to provide the production services to the THCs for a fee fixed at only 80.1% of their cost. The PLPs fixed that fee at 80.1% of cost without any negotiation, contrary to industry standards and without any business rationale. The PLPs selected 80.1% in an attempt to avoid the matchable expenditures rules in section 18.1 of the *Act* while maximizing the losses created.

7. The PLPs therefore committed to providing production services to the THCs at 80.1% of their cost while agreeing to pay the Studios that cost plus a mark-up to provide those services. To overcome this guaranteed loss with the appearance of a profit potential, the PLP production services contracts included a Net Profit Participation or NPP clause.

8. While creating an appearance of a profit potential , the Net Profit Participations were structured and intended to be, and were in fact, worthless. There was no prospect that the PLPs would receive any amount from the Net Profit Participation must less produce a profit. The Net Profit Participations were at best mere window-dressing.

9. The clients of the Promoters, the Canadian resident Investors, including the appellant, acquired units in the MLP and the MLP allocated losses created in the PLP to the Investors as detailed in Schedule A to this Reply.

10. The Investors acquired units in the MLP through financing arrangements that were as circular as the production services contracts and which guaranteed that no funds beyond their actual cash were ever at risk.

11. The cash contributed by the Investors to acquire units of the MLPs was used to pay the fees of the Promoters, the accommodating Studios, and other "accommodators," not to pay for production services provided to the THCs. The MLP and PLPs created the appearance of working capital through a series of circular daylight "loans". In fact, there was no working capital.

12. The Promoters ensured that any supposed liabilities of the Investors beyond the cash actually contributed was eliminated by inserting into the tax loss creation scheme "options" in favour of the Studios. These "options" were sham transactions designed to mislead the CRA as to the genuine nature of the transactions. These "options" were designed to limit the amount at risk of the Investors. The "options" were not optional. Rather, the parties treated the "options" as mandatory in order to fulfill the real agreement of renting the Studio's expenditures.

13. The units acquired by the Investors were not genuine partnership units. They were known by the Studios, the promoters and the Investors to be worthless. The scheme was designed to benefit the Investors who purchased tax losses, the promoters who received fees for arranging those purchases, and the Studios who received a premium for renting their expenditures. The tax loss creation scheme was not designed to produce a profit in either the MLP or the PLPs.

14. The transactions comprising the tax loss scheme were designed to create the appearance of a genuine partnership in pursuit of profit when the true relationship was decidedly different. The true relationship of the parties was simply the renting of expenses, which does not give rise to a deductible tax loss.

15. As the sole intention and purpose of the members of the MLP and the PLPs was to create losses through an intricate series of circular transactions, and not to carry on business in common with a view to profit, the MLP and PLPs were not partnerships in law.

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COURT FILES NOS.:	2007-329(IT)G, 2009-2247(IT)G and 2009-2248(IT)G
STYLES OF CAUSE:	ROBERT STROTHER v. THE QUEEN SENTINEL HILL PRODUCTIONS IV CORPORATION, IN ITS CAPACITY AS DESIGNATED MEMBER OF SENTINEL HILL NO. 207 LIMITED PARTNERSHIP v. THE QUEEN SENTINEL HILL PRODUCTIONS IV CORPORATION, IN ITS CAPACITY AS DESIGNATED MEMBER OF SHAAE (2001) MASTER LIMITED PARTNERSHIP v. THE QUEEN
PLACE OF HEARING:	Toronto, Ontario
DATE OF HEARING:	September 22, 2010
REASONS FOR ORDER BY:	The Honourable Gerald J. Rip, Chief Justice
DATE OF ORDER:	May 12, 2011

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