Date: 20080917

Docket: T-1056-02

Citation: 2008 FC 1037

Ottawa, Ontario, September 17, 2008

PRESENT: The Honourable Mr. Justice O'Reilly

BETWEEN:

IMPERIAL OIL RESOURCES LIMITED,
IMPERIAL OIL RESOURCES VENTURES LIMITED

Plaintiffs

and

THE ATTORNEY GENERAL OF CANADA

Defendant

REASONS FOR JUDGMENT AND JUDGMENT

I. Overview

[1] Governments use various financial incentives to encourage companies to engage in desirable conduct. A common one is to provide tax advantages for devoting resources to particular activities. Another is to provide a discount on fees payable to the government in return for a desired capital investment. This case involves the intersection of the two.

[2] Generally speaking, I will refer to the plaintiffs jointly as "Imperial". Where the context requires otherwise, I will refer to Imperial Oil Resources Limited as "IORL" and Imperial Oil Resources Ventures Limited as "IORVL".

[3] The government of Canada and the government of Alberta both encouraged Imperial, and others, to develop a valuable resource – the oil sands in the Athabaska region near Fort McMurray, Alberta. In 1976, the federal government agreed to remit to Imperial income taxes it would otherwise have had to pay according to amendments to the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.), that had been enacted the previous year. These amendments are referred to as the "royalty provisions". The tax remission related solely to development of the oil sands, a venture called the Syncrude Project. Later, in the 1990s, Alberta gave Imperial a discount on the royalties it would otherwise have had to pay Alberta on the condition that Imperial invest in an expansion of the Syncrude Project. Since 2001, Imperial and the Minister of Revenue have disagreed on the effect, if any, that the Alberta incentive should have on the amount of income tax remitted to Imperial.

[4] The royalty provisions were enacted just prior to the signing of the Syncrude Agreement, which created the Syncrude Project. These provisions changed the tax treatment of royalties that mining companies were paying to provincial governments. While royalties had previously been *deductible* from income, the amendments required companies to *include* royalties in income. The purpose of the amendments was to immunize the federal tax base from changes in provincial royalty schemes. Prior to the amendments, if provincial royalties rose, mining companies paid less federal income tax because the royalties were deductible from income. After the amendments, companies

were no longer permitted to deduct royalties from income. So, if provincial royalties went up, there was no effect on the amount of income tax the federal government received. From the perspective of the companies affected, the net effect of the amendments was to increase their income tax in an amount equivalent to the tax payable on the royalties paid to the provinces (although the effect was somewhat alleviated by a resource allowance deduction).

[5] However, participants in the Syncrude Project were treated differently. Under the Syncrude Remission Order (SRO), enacted in 1976, they were granted remission on the tax that they would otherwise have had to pay on those provincial royalties. In other words, participants in the Syncrude Project were treated as if the royalty amendments to the *Income Tax Act* had never been enacted. This tax remission served as a financial incentive to develop the oil sands. This arrangement was clear and uncontroversial for at least two decades.

[6] Two things happened in the mid-1990s that complicated matters. First, the participants in the Syncrude Project, including Imperial, expanded their operations. In addition to the mining leases that defined the original project (called Leases 17 and 22), the participants acquired other leases (called the Aurora leases). The combined operation is called the Expanded Syncrude Project. Second, Alberta agreed to treat the Expanded Syncrude Project (*i.e.*, Leases 17 and 22 and the Aurora leases) as a single unit for purposes of calculating the royalties that the participants owed to the province. This meant that part of the capital investment that the participants made in developing the Aurora leases was subtracted from the royalties that they had to pay Alberta. In other words, the

participants achieved a discount on their royalties to encourage their investment in the Expanded Syncrude Project. The parties refer to this discount as the "Aurora credits".

[7] The question that arises from these developments is how to calculate the amount of tax remission owed to Imperial (and the other participants) in subsequent years. The parties propose different answers to that question. Imperial says the Minister's answer creates a shortfall. The Minister says Imperial's answer creates a windfall.

II. Summary of Arguments

[8] Imperial argues that the method of calculating the tax remission should remain essentially the same as that contemplated under the original SRO. It submits that the remission should be based on the royalty amount that would have been payable to Alberta in respect of the original leases alone, even though the actual royalty that it was paying to Alberta was determined in respect of the Expanded Syncrude Project and, because of the Aurora credits, was lower than the royalties payable in respect of the original Syncrude Project. This methodology is described as "ring-fencing" given that it involves treating the original Syncrude leases as a completely discrete project, separate and apart from the leases that were added to form the expanded project.

[9] The Minister suggests that Imperial's position produces a bonus resulting from the fact that the royalty for the expanded project is less than the royalty for the original leases. Therefore, the amount of the remission Imperial is seeking exceeds the amount of tax it paid on the royalty that it

actually owed. The Minister argues that the remission to which Imperial is entitled should be based on the royalty paid to Alberta in respect of the Expanded Syncrude Project, not a "notional" royalty calculated as if the oil sands development were still confined to the original leases. The Minister also submits that Imperial's position is out of keeping with the concept of a "remission", as well as the terms of the *Financial Administration Act*, R.S., 1985, c. F-11, the SRO, and the *Income Tax Act*. In the alternative, the Minister argues that, if Imperial's interpretation is correct, then it realized an unjust enrichment that should be calculated and taxed as income.

[10] For the taxation year 1997, Imperial's claim for remission, based on the foregoing methodology, was denied by the Minister. Instead, the Minister granted remission based on the amount of the royalty Imperial actually paid to Alberta in respect of the Expanded Syncrude Project. In this action, Imperial seeks to recover the remission amounts it was denied, plus interest. The treatment of other taxation years and other Syncrude participants is the subject of other pending actions.

[11] Therefore, the main issue is:

- What is the proper way to calculate the amount of tax remission to which Imperial was entitled for the year 1997?

[12] A secondary issue arises if I find that Imperial's proposed methodology is correct:

- Should the discount Imperial realized on its royalty payments to Alberta be taxed as an "inducement" under s. 12 (1)(*x*) of the Act?

[13] I agree with Imperial that its methodology is correct. I have also concluded that Imperial did not realize a taxable benefit. Therefore, I must allow Imperial's action.

III. Factual Background

1. The Syncrude Project

[14] Mr. Robert Wilson, who was a manager at Imperial for 35 years, mainly in the oil sands business, described the history of the Syncrude Project and the process by which synthetic crude oil is extracted from sand. The Syncrude Project began in the mid-1970s and involved development of mines on the west side of the Athabasca River. It has three main components: the mining operation; the extraction process, which involves separating bitumen from the sand; and an upgrader, which refines the bitumen into synthetic crude.

[15] The mining operation amounts to removing ore from the ground with shovels and trucks. The ore is taken to dumping facilities where it is crushed. About 11% of the crushed ore is bitumen. To extract the bitumen, the ore is mixed with hot water and, after a separation process, a froth is produced, consisting of about 60% bitumen, 30% water and 10% solids. The froth is sent by pipeline to an upgrader, where it is refined into synthetic crude. All of this takes place on the site of

the original project (*i.e.*, Leases 17 and 22). The facilities were expanded in the late 1990s to prepare for processing the ore from the Aurora leases.

2. The Syncrude Remission Order (SRO)

[16] As mentioned, prior to 1974, when calculating their liability under the *Income Tax Act*, mining companies could deduct from their income the amounts paid to the provinces as royalties. However, thereafter provincial royalties were no longer deductible from income (see ss. 12(1)(*o*) and 18(1)(*m*); enactments cited are set out in Annex A). The participants in the Syncrude Project were given tax relief from the new royalty provisions by way of the SRO. The intent of the SRO was to put the participants in the same position they would have occupied if the royalty provisions had never been enacted.

[17] Subsection 3(1)(*b*) of the SRO states that "remission is hereby granted to each participant of any tax payable . . . as a result of the royalty provisions being applicable to . . . a royalty. . . with respect to the Syncrude Project . . ." (See Annex B).

[18] In effect, then, the Syncrude participants were obliged to include in their income the amounts they were paying to Alberta as royalties, but were entitled to be compensated, in the form of a tax remission, for the tax they paid on those amounts. The parties do not disagree about the purposes of the royalty provisions of the *Income Tax Act* or the SRO. Those purposes were described in statements and letters of Ministers of Finance of the day. For example, the Honourable

Donald Macdonald stated in a letter to the Syncrude participants dated April 26, 1976 that the government was committed "to exclude from your company's income any amounts derived from the Syncrude Project by the federal or provincial governments" and that the commitment "would be given effect via remission order". Further, an advance ruling from Revenue Canada made clear that the effect of the remission order would be to make the amounts paid to Alberta as a royalty in respect of the Syncrude Project non-taxable.

[19] The royalties paid to Alberta by participants in the Syncrude Project were established under the Alberta Crown Agreement (ACA) of 1975. Under the ACA, Alberta was entitled to receive half of the Syncrude Project's Deemed Net Profit. Until the mid-1980s, Alberta took its royalties in kind (*i.e.*, in oil). Thereafter, it received its royalties in cash.

[20] No serious issue about this arrangement arose until the mid-1990s when the Syncrude Project expanded and Alberta changed its royalty regime.

3. Changes to the Alberta Crown Agreement (ACA)

[21] In the mid-1990s Alberta introduced a "generic royalty regime" which calculated royalties at 25% of net profit. The generic system applied to all companies involved in oil sands production. Previously, royalties were established project by project. By way of a 1997 agreement with the Syncrude participants, referred to as Amendment No. 6, the new regime applied to the Expanded Syncrude Project as described below.

4. The Expanded Syncrude Project

[22] In 1994 and 1996, three new leases (the Aurora leases) were added to the Syncrude Project. They are located about 30 kilometres north of Leases 17 and 22. The Aurora leases did not come into production until 2000.

[23] At the time of this expansion, the Syncrude participants asked Alberta to treat the expanded Syncrude Project as a single entity for purposes of calculating the royalties owing to Alberta under its new "generic royalty regime". Alberta agreed. That agreement is reflected in Amendment No. 6 to the ACA which includes a formula for calculating royalties based on Alberta's new generic approach.

[24] The royalty formula (see Annex C) allows capital credits to reduce the amount of royalty payable. In essence, the capital credits are subtracted from the Deemed Net Profit for the Expanded Syncrude Project to arrive at Alberta's share. So, during the years when Imperial was realizing a profit from production at the original Syncrude Project, and it was making capital investments in the Aurora leases, its royalty payment to Alberta was less than it would otherwise have been if its operations had been confined to Leases 17 and 22. Clearly, this was the intention – to create a financial incentive for the participants to expand their oil sands development. Under Alberta's royalty formula, the amount of royalty paid on the expanded project was discounted by a proportion

(43%) of the capital investment in the development of the Aurora leases. That discount is called the Aurora credits.

IV. What is the proper way to calculate the amount of tax remission to which Imperial was entitled for the year 1997?

1. The Parties' Positions

[25] The parties provided helpful tables illustrating their respective positions, and comparing them with the situation before and after enactment of the royalty provisions and the SRO. I will reproduce parts of them here to show the differences in their positions. The tables are based on simplified figures, not the actual amounts in issue here. I will come to the actual amounts later.

TABLE 1 – POSITIONS OF THE PARTIES

	Column 1	Column 2	Column 3	Column 4
Description	**Tax payable prior to enactment of royalty amendments**	**Tax payable after enactment of royalty amendments (no SRO)**	**Tax payable under SRO (per Minister)**	**Tax payable under SRO (per Imperial)**
Gross Revenue	$1500	$1500	$1500	$1500
Crown Royalty	(100)	(100)	(100)	(100)
Operating expense	(800)	(800)	(800)	(800)
Net accounting income	600	600	600	600
Add: Crown Royalty (s. 12(1)(*o*))	n/a	100	100	100
Taxable Income before SRO	600	700	700	700
Royalty eligible for remission	n/a	n/a	(100)	(120)
Revised income	600	700	600	580
Tax:				
Base amount – 38%	228.00	266.00	228.00	220.40
Abatement – 10%	(60)	(70)	(60)	(58)
Surtax – 4%	6.72	7.84	6.72	6.50
Tax payable	**$174.72**	**$203.84**	**$174.72**	**$168.90**

[26] This simplified example shows that, prior to the enactment of the royalty provisions, Imperial would have reduced its income by the amount of the royalty paid to Alberta ($100) and would have been taxed on the remainder ($600) (Column 1).

[27] The royalty provisions would have obliged Imperial to add the amount of the royalty ($100) back onto its income and Imperial would have been taxed on the higher amount ($700) (Column 2).

[28] After the SRO was enacted, according to the Minister, Imperial was entitled to subtract the $100 royalty from its income calculated according to the royalty provisions and, once again, be

taxed on the lower amount ($600) (Column 3). The Minister submits that this calculation shows that the SRO achieved its purpose of treating the Syncrude participants as if the royalty provisions had never been enacted. Imperial's tax liability would have been the same before the amendments were enacted (Column 1) as it was after (Column 3), due to the effect of the SRO.

[29] Column 4 represents Imperial's position regarding the effect of Amendment No. 6. Under Amendment No. 6, Imperial paid a royalty to Alberta based on the Expanded Syncrude Project. In this example, that royalty was $100. However, Imperial maintains that the SRO required it to calculate what the royalty would have been on the original Syncrude leases given that the SRO defined the Syncrude Project as being limited to those areas. Imperial calculated the royalty amount for the original leases as being, in this example, $120. So, as reflected in the calculation in Column 4, Imperial actually paid a royalty to Alberta of $100 and then, as it was required to do according to the royalty provisions, added that amount to its income. However, it then subtracted from its income the royalty it claims was eligible for remission ($120), the amount of royalty corresponding to production at the original leases, *i.e.*, the original Syncrude Project. This calculation results, in this example, in a tax saving to Imperial of $5.82 as compared to the Minister's position (comparing Column 4 with Column 3).

2. The "Two-Return" Method

[30] The parties agree that the proper way to calculate Imperial's tax liability is the "two-return" method (according to the approach set out in *Perley* v. *The Queen*, [1999] F.C.J. No. 461 (F.C.A.)

(QL)). This simply means that Imperial must prepare one tax return that reflects its tax liability according to the *Income Tax Act*, including the royalty provisions. It must then prepare a second return that takes account of the SRO. The difference between the two is the amount of tax remission to which Imperial is entitled. The parties disagree on how to prepare the second return.

[31] While the same information is included above in Table 1, I will reproduce it here for ease of reference:

TABLE 2 – THE "TWO-RETURN" METHOD

	Column 1	**Column 2**	**Column 3**
Description	**Return 1: Tax payable according to the Income Tax Act, including royalty provisions**	**Return 2: Tax payable under SRO (per Minister)**	**Return 2: Tax payable under SRO (per Imperial)**
Gross Revenue	$1500	$1500	$1500
Crown Royalty	(100)	(100)	(100)
Operating expense	(800)	(800)	(800)
Net accounting income	600	600	600
Add: Crown Royalty (s. 12(1)(o))	100	100	100
Taxable Income before SRO	700	700	700
Royalty eligible for remission	**n/a**	**(100)**	**(120)**
Revised income	700	600	580
Tax:			
Base amount- 38%	266.00	228.00	220.40
Abatement – 10%	(70)	(60)	(58)
Surtax – 4%	7.84	6.72	6.50
Tax payable	**$203.84**	**$174.72**	**$168.90**

[32] The difference between Column 1 and Column 2 ($29.12) is the amount of remission to which Imperial was entitled (and allowed), according to the Minister. The difference between Column 1 and Column 3 ($34.94) is the amount of remission to which Imperial says it was entitled. The difference between Column 2 and Column 3 ($5.82) is, in our example, the amount Imperial is claiming in this action.

[33] As one can clearly see, the dispute between the parties relates solely to the amount of royalty eligible for remission (see the row "Royalty eligible for remission" set out in bold in Table 2). According to the Minister, the amount of royalty eligible for remission is the same amount that Imperial included in its income ($100). This represents, in this example, the amount of royalty that Imperial actually paid to Alberta in respect of the Expanded Syncrude Project under the terms of Amendment No. 6, taking into account the Aurora credits. By contrast, according to Imperial, it was required to include in its income the amount of the royalty that it paid to Alberta in respect of the Expanded Syncrude Project ($100). However, Imperial also maintains that, by virtue of the SRO, it was entitled to deduct from its income the amount of the royalty that would have been payable in respect of the original leases ($120), an amount unreduced by the Aurora credits.

3. Interpretation of the SRO

[34] To determine the proper means of calculating the remission Imperial was owed, one must start with the SRO. The key provision of the SRO is paragraph 3(1)(*a*). To repeat, it provides that "remission is hereby granted to each participant of any tax payable . . . as a result of the royalty

provisions being applicable to . . . a royalty. . . with respect to the Syncrude Project . . .” (See Annex B).

[35] To paraphrase, the SRO provides that Imperial is entitled to remission on the additional tax payable as a result of having to include in its income royalties connected to the Syncrude Project. The object of the SRO was to relieve Imperial and the other participants from the tax effect that the royalty provisions would have had on the Syncrude Project. The SRO defines the Syncrude Project as being confined to the original leases.

[36] Given its wording and purpose, it is a relatively easy exercise to calculate the amount of remission provided by the SRO. First, one must determine the amount of the royalty connected to the Syncrude Project as originally conceived. In the example above, this amount is $120.00. Second, one must determine the effect of the royalty provisions. As mentioned, the royalty provisions rendered royalty payments non-deductible. Mining companies were required to include royalties in their income. So, after the royalty provisions came into effect, given that the royalty payment for the Syncrude Project was no longer deductible, Imperial’s income would have included the $120 that was payable as a royalty to Alberta for the Syncrude Project (even though the amount actually paid to Alberta was discounted by the Aurora credits). Third, one must calculate the amount of tax Imperial would have to pay on that additional income. That amount is the amount of remission to which Imperial was entitled. According to the tax rates included in the above tables, the tax payable on $120.00 is:

Base amount – 38%	=	$45.60
Abatement – 10%	=	($12.00)
Surtax – 4%	=	$1.34
Tax payable	=	**$34.94**

[37] The amount of $34.94 is the amount of remission Imperial claims it was owed (using hypothetical figures). The methodology Imperial proposes for the application of the SRO yields this same figure and I find, therefore, that it is correct. Imperial's calculation can be seen in Column 4 of Table 1 or Column 3 of Table 2. It simply involves deducting $120.00 from Imperial's income, being the amount of the royalty associated with the Syncrude Project.

4. Real Numbers

[38] In keeping with the methodology described above, the plaintiffs added to their income for 1997 the actual amount paid to Alberta as a royalty in respect of the Expanded Syncrude Project, as calculated according to Amendment No. 6. For Imperial Oil Resources Limited (IORL), this amount was $28,206,000; for Imperial Oil Resources Ventures Limited (IORVL), the amount was $74,358,000. Each of the companies then deducted from income the amount of the royalty attributable to the original Syncrude Project, being $28,344,000 for IORL and $74,723,000 for IORVL.

[39] The Minister granted the plaintiffs remission on the tax payable on the lower amounts but denied their proposed deduction of the higher. The Minister allowed remission of $8,215,043 to IORL and $21,656,835 to IORVL. The plaintiffs argue that they are entitled to remission based on

the higher amount. The shortfall, they say, is $41,059 for IORL and $107,744 for IORVL.

[40] In keeping with the methodology described above, I agree with Imperial that it was entitled to deduct from its income the amount of the royalty associated with the original Syncrude Project, being $28,344,000 for IORL and $74,723,000 for IORVL. In turn, the companies were entitled to the corresponding amount of remission and are owed the sums denied them by the Minister.

5. The Minister's Submissions

[41] While the Minister's position is multi-faceted, it can be expressed simply. The Minister submits that the royalty eligible for remission under the SRO must be the same as the royalty included in income pursuant to the royalty provisions of the *Income Tax Act*. Accordingly, if the original Syncrude Project is to be ring-fenced for purposes of the SRO, so must it be for purposes of the *Income Tax Act*; the amount included in income must be the same as the amount deducted from income. As one can see from the Minister's calculations in Table 1 (Column 3) and Table 2 (Column 2), the amount added to income as a Crown royalty ($100) is the same as the amount subtracted from income as the royalty eligible for remission ($100).

[42] If it were otherwise, the Minister contends, Imperial would realize a windfall, unintended by the parties to the Syncrude Agreement and contrary to the purposes of the SRO. Worse, perhaps, Imperial would enjoy a partial tax holiday on profits it realized from its oil sands operations.

[43] In support of his position, the Minister submits that the royalty provisions, specifically s. 12(1)(*o*) of the *Income Tax Act*, require Imperial to include in its income the amount of the royalty that was actually "receivable" by Alberta, not a "notional" amount corresponding only to Leases 17 and 22. The Minister argues that, to be "receivable", a person must have a legal right to receive it (citing *M.N.R.* v. *John Colford Contracting Company Limited*, 60 D.T.C. 1131 (Ex. Ct.) at 1135; *Maple Leaf Mills Limited* v. *M.N.R.*, 76 D.T.C. 6182 (S.C.C.); *West Kootenay Power & Light Co.* v. *Her Majesty the Queen*, 92 D.T.C. 6023 (F.C.A.)). Further, he notes that the "royalty" must be in relation to actual production, not an abstract calculation based on notional figures.

[44] It is clear from these requirements, according to the Minister, that the amount Imperial includes in its income must be the amount actually owed, by law, by Imperial to Alberta in respect of its oil sands production. That amount, in the example above, would be $100. Imperial, to this point, agrees.

[45] However, the Minister goes on to suggest that the same words ("receivable" and "royalty") must be given the same meaning when reading the SRO. To repeat, the SRO gives remission on the tax payable as a result of the application of the royalty provisions of the *Income Tax Act*. It specifies that the remission relates to the tax arising from the amount "receivable" by the Crown as a "royalty". The Minister contends, once again, that the amount "receivable" by Alberta as a "royalty" was the amount Imperial owed to Alberta, by law, in respect of its oil sands development. And, in our example, this would be $100, the same amount as would be included in Imperial's income

pursuant to s. 12(1)(*o*) of the *Income Tax Act*.

[46] The symmetry and logic of the Minister's submission is appealing, but I cannot agree with it. While the words "receivable" and "royalty" can be given the same meaning in the Act and the SRO, this cannot change the fact that the two instruments are addressing different things. The Act contains a general provision requiring royalties to be included in income. The SRO contains specific relief against the tax payable on royalties for the Syncrude Project as originally conceived. So, the Act requires inclusion of a "royalty" "receivable" by Alberta, while the SRO allows remission of the tax payable on the "royalty" "receivable" by Alberta "with respect to the Syncrude Project". In my view, Imperial's claim for remission flows from the intersection of the general requirement of the Act and the specific remedy of the SRO. Its claim is consistent with the purpose for which the royalty provisions were enacted – to uncouple federal tax liability from provincial royalty arrangements. According to Imperial's approach, its federal tax situation remained the same notwithstanding the changes in Alberta's royalty regime. The federal government was no worse off as a result. It seems to me that, just as the royalties attributable to profits at Aurora are not eligible for remission under the SRO, nor should the Aurora credits be used to reduce the eligible royalty.

V. Should the discount on Imperial's royalty payments to Alberta be subject to tax under s. 12(1)(*x*) of the Act?

[47] As an alternative argument, the Minister submits that if Imperial's interpretation of the *Income Tax Act* and the SRO is correct, then Imperial was unjustly enriched and should be taxed on

an amount equal to the "excess" remission it receives. That "excess" is a product of the difference between the royalty attributed to the original Syncrude Project and the royalty actually paid to Alberta in respect of the Expanded Syncrude Project. Given that the difference between the two figures is a function of the capital credits Imperial earned for its investment on the Aurora leases, the Minister contends, in effect, that Imperial should be taxed on the Aurora credits.

[48] As stated at the beginning of these reasons, it is clear that Alberta offered Imperial a financial incentive to expand its oil sands operations. The question is whether that incentive can be characterized as an "inducement" or a "grant" and taxed accordingly under s. 12(1)(*x*) of the Act. Imperial argues that the Aurora credits are an integral element in the calculation of its royalty obligation – it cannot be isolated, removed from the equation and characterized separately from it. The Minister actually agrees with that position, to a point. Counsel for the Minister stated that Imperial is correct in saying that "the credit is an integral part of the calculation of the royalty and, if that is true, we agree [that] s. 12(1)(*x*) does not apply".

[49] The Minister argues that the Aurora credits should be regarded as an integral part of the calculation of the royalty payment to Alberta and, therefore, that the royalty eligible for remission should be reduced accordingly. I have already concluded that the royalty eligible for remission should not be reduced by the Aurora credits. The Minister offers, then, the alternative argument that, if the Aurora credits are to be severed for purposes of calculating the royalty eligible for remission, then they should be regarded as a taxable inducement.

[50] Again, I cannot accept the Minister's submission. True, the Aurora credits form no part of the calculation of the royalty relating to the Syncrude Project, as originally conceived and defined. However, they do form an integral part of the royalty formula for the Expanded Syncrude Project. It would be incorrect, and unfair, in my view, to carve them off from the rest of the equation and treat them as a free-standing, taxable payment from Alberta to Imperial.

[51] Alberta and Imperial agreed on a royalty calculation that included partial credit (not full deductibility) for Imperial's capital investment in an expansion of its oil sands operations. That agreement gave Imperial only partial compensation for its capital investment, but at a level, one assumes, sufficient to cause Imperial to devote its resources to the project and yet low enough for Alberta to derive a correspondingly satisfactory public benefit in terms of the product produced, the wealth generated and the profits it shared. Alberta did not give Imperial a "grant" in return for Imperial's commitment. It negotiated and signed a deal that included multiple variables, some to Imperial's advantage and some to Alberta's, but none of which can fairly be isolated from the rest and characterized separately. Certainly not the Aurora credits. The royalty payable on the expanded project was lowered during the years before Aurora came into production and, presumably, rose thereafter. The benefit to Imperial was temporary and likely recaptured soon after Aurora started yielding crude.

[52] As I see it, the Aurora credits form no part of the royalty calculation for the Syncrude Project (and, therefore, do not figure in determining the royalty eligible for remission under the SRO), yet form an integral part of the royalty calculation for the Expanded Syncrude Project (and,

therefore, cannot be characterized as a form of taxable inducement or grant under s. 12(1)(*x*) of the Act).

[53] I heard expert evidence from both parties on the economic gain that Imperial would realize if I accepted its approach to calculating its remission entitlement. Because I have concluded that this amount does not fall within s. 12(1)(*x*), it is unnecessary for me to quantify it.

VI. Interest

[54] Imperial seeks interest on the unpaid remissions to which it is entitled. While initially opposed, questioning the legal authority for an order relating to interest and Imperial's equitable entitlement to it, the Minister conceded at the hearing that interest was payable according to the *Crown Liability and Proceedings Act*, R.S.C. 1980, c. C-50, s. 31(2). In my view, interest on unpaid remission is payable and should be set at an amount comparable to the rate prescribed for refunds under the *Income Tax Act*.

JUDGMENT

THIS COURT'S JUDGMENT is that

1. The Minister remit to IORL payment in the amount of $41,059.00, to which it is entitled for the 1997 taxation year pursuant to the Syncrude Remission Order;

2. The Minister remit to IORVL payment in the amount of $107,744.00, to which it is entitled for the 1997 taxation year pursuant to the Syncrude Remission Order;

3. The Minister pay interest on the amounts ordered at the rate prescribed for refunds under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.); and

4. The plaintiffs are entitled to costs.

"James W. O'Reilly"
Judge

Annex « A »

Income Tax Act, R.S.C. 1985, C. 1

Income inclusions

12. (1) There shall be included in computing the income of a taxpayer for a taxation year as income from a business or property such of the following amounts as are applicable

Services, etc., to be rendered

[…]

(*o*) Royalties, etc., to be included in income, -- any amount (other than an amount referred to in paragraph 18(1)(*m*), paid or payable by the taxpayer, or a prescribed amount) that became receivable in the year by virtue of an obligation imposed by statute or a contractual obligation substituted for an obligation imposed by statute by

(i) her Majesty in right of Canada or a province,

(ii) an agent of Her Majesty in right of Canada or a province, or

(iii) a corporation, commission or association that is controlled, directly or indirectly in any manner whatever, by Her Majesty in right of Canada or a province or by an agent of Her Majesty in right of Canada or a province

As a royalty, tax (other than a tax or portion thereof that may reasonably be considered to be a municipal or school tax), lease rental or bonus or as an amount, however described, that may reasonably be regarded as being in lieu

Loi sur l'impôt, L.R.C. 1985, ch. 1

Sommes à inclure dans le revenu

12. (1) Sont à inclure dans le calcul du revenu tiré par un contribuable d'une entreprise ou d'un bien, au cours d'une année d'imposition, celles des sommes suivantes qui sont applicables :

Services à rendre

…

o) Les redevances, etc. sont incluses dans le revenue. – toute somme (autre qu'une somme visée à l'alinéa 18(1)(*m*), payée ou payable par le contribuable, ou une somme prescrite), devenue recevable au cours de l'année en vertu d'une obligation imposée par une loi ou d'une obligation contractuelle qui remplace une obligation imposée par une loi

(i) par Sa Majesté du chef du Canada ou d'une province,

(ii) par un mandataire de Sa Majesté du chef du Canada ou d'une province, ou

(iii) par une corporation, commission ou association contrôlée directement ou indirectement, de quelque façon que ce soit, par Sa Majesté du chef du Canada ou d'une province ou par un mandataire de Sa Majesté du chef du Canada ou d'une province

À titre de redevance, de taxe (autre qu'une taxe ou fraction de taxe qui peut raisonnablement être considérée comme une taxe municipale ou scolaire), de loyer, de prime, ou à titre de somme, quelle que soit la façon dont elle est désignée, qui peut être raisonnablement considérée comme tenant lieu d'une telle somme, qui

of any such amount, and that may reasonably be regarded as being in relation to
(iv) the acquisition, development or ownership of a Canadian resource property or a property that would have been a Canadian resource property if it had been acquired after 1971, or
(v) the production in Canada of
(A) petroleum, natural gas or related hydrocarbons from a mineral resource or an oil or gas well, or
(B) metal or minerals, to any stage that is not beyond the prime metal stage or its equivalent, from a mineral resource
Situated on property in Canada in which the taxpayer had an interest with respect to which the obligation imposed by statute or the contractual obligation, as the case may be, applied;

peut raisonnablement être considérée comme rattachée
(iv) à l'acquisition, à l'aménagement ou à la propriété d'un avoir minier canadien ou d'un bien qui aurait été un avoir minier canadien s'il avait été acquis après 1971, ou
(v) à la production au Canada
(A) de pétrole, de gaz naturel ou d'hydrocarbures apparentés tirés de ressources minérales ou d'un puis de pétrole ou de gaz, ou
(B) de métaux ou de minerai, jusqu'à un stade ne dépassant pas celui du métal primaire ou de son équivalent, tirés de ressources minérales
situées au Canada sur un bien dans lequel le contribuable avait une participation assujettie à l'obligation imposée par une loi ou à l'obligation contractuelle, selon le cas;

Inducement, reimbursement, etc.

(*x*) any particular amount (other than a prescribed amount) received by the taxpayer in the year, in the course of earning income from a business or property, from

(i) a person or partnership (in this paragraph referred to as the "payer") who pays the particular amount

(A) in the course of earning income from a business or property,

(B) in order to achieve a benefit or advantage for the payer or for persons with whom the payer does not deal at arm's length, or

Paiements incitatifs et autres

x) un montant (à l'exclusion d'un montant prescrit) reçu par le contribuable au cours de l'année pendant qu'il tirait un revenu d'une entreprise ou d'un bien :

(i) soit d'une personne ou d'une société de personnes (appelée « débiteur » au présent alinéa) qui paie le montant, selon le cas :

(A) en vue de tirer un revenu d'une entreprise ou d'un bien,

(B) en vue d'obtenir un avantage pour elle-même ou pour des personnes avec qui elle a un lien de dépendance,

(C) dans des circonstances où il

(C) in circumstances where it is reasonable to conclude that the payer would not have paid the amount but for the receipt by the payer of amounts from a payer, government, municipality or public authority described in this subparagraph or in subparagraph (ii), or

(ii) a government, municipality or other public authority,

where the particular amount can reasonably be considered to have been received

(iii) as an inducement, whether as a grant, subsidy, forgivable loan, deduction from tax, allowance or any other form of inducement, or

(iv) as a refund, reimbursement, contribution or allowance or as assistance, whether as a grant, subsidy, forgivable loan, deduction from tax, allowance or any other form of assistance, in respect of

(A) an amount included in, or deducted as, the cost of property, or

(B) an outlay or expense,

to the extent that the particular amount

(v) was not otherwise included in computing the taxpayer's income, or deducted in computing, for the purposes of this Act, any balance of undeducted outlays, expenses or other amounts, for the year or a

est raisonnable de conclure qu'elle n'aurait pas payé le montant si elle n'avait pas reçu des montants d'un débiteur, d'un gouvernement, d'une municipalité ou d'une autre administration visés au présent sous-alinéa ou au sous-alinéa (ii),

(ii) soit d'un gouvernement, d'une municipalité ou d'une autre administration,

s'il est raisonnable de considérer le montant comme reçu :

(iii) soit à titre de paiement incitatif, sous forme de prime, de subvention, de prêt à remboursement conditionnel, de déduction de l'impôt ou d'indemnité, ou sous toute autre forme,

(iv) soit à titre de remboursement, de contribution ou d'indemnité ou à titre d'aide, sous forme de prime, de subvention, de prêt à remboursement conditionnel, de déduction de l'impôt ou d'indemnité, ou sous toute autre forme, à l'égard, selon le cas :

(A) d'une somme incluse dans le coût d'un bien ou déduite au titre de ce coût,

(B) d'une dépense engagée ou effectuée,

dans la mesure où le montant, selon le cas :

(v) n'a pas déjà été inclus dans le calcul du revenu du contribuable ou déduit dans le calcul, pour

preceding taxation year,

(vi) except as provided by subsection 127(11.1), 127(11.5) or 127(11.6), does not reduce, for the purpose of an assessment made or that may be made under this Act, the cost or capital cost of the property or the amount of the outlay or expense, as the case may be,

(vii) does not reduce, under subsection 12(2.2) or 13(7.4) or paragraph 53(2)(s), the cost or capital cost of the property or the amount of the outlay or expense, as the case may be, and

(viii) may not reasonably be considered to be a payment made in respect of the acquisition by the payer or the public authority of an interest in the taxpayer or the taxpayer's business or property;

l'application de la présente loi, d'un solde de dépenses ou autres montants non déduits, pour l'année ou pour une année d'imposition antérieure,

(vi) sous réserve des paragraphes 127(11.1), (11.5) ou (11.6), ne réduit pas, pour l'application d'une cotisation établie en vertu de la présente loi, ou pouvant l'être, le coût ou le coût en capital du bien ou le montant de la dépense,

(vii) soit il ne réduit pas, en application du paragraphe (2.2) ou 13(7.4) ou de l'alinéa 53(2)s), le coût ou coût en capital du bien ou le montant de la dépense,

(viii) soit on ne peut raisonnablement le considérer comme un paiement fait au titre de l'acquisition par le débiteur ou par l'administration d'un droit sur le contribuable, sur son entreprise ou sur son bien;

General limitations

18. (1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of

[…]

(*m*) Royalties, etc. – any amount (other than a prescribed amount) paid or payable by virtue of an obligation imposed by statute or a contractual obligation substituted for an obligation imposed by statute to

(i) Her Majesty in right of Canada or a province,

(ii) an agent of Her Majesty in right of Canada or a province, or

Exceptions d'ordre général

18. (1) Dans le calcul du revenu du contribuable, tiré d'une entreprise ou d'un bien, les éléments suivants ne sont pas déductibles

…

m) Redevances, etc. – toute somme (autre qu'une somme prescrite)payée ou payable en vertu d'une obligation imposée par une loi ou d'une obligation contractuelle qui remplace une obligation imposée par une loi

(i) à Sa Majesté du chef du Canada ou d'une province,

(iii) a corporation, commission or association that is controlled, directly or indirectly in any manner whatever, by Her Majesty in right of Canada or a province or by an agent of Her Majesty in right of Canada or a province

As a royalty, tax (other than a tax or portion thereof that may reasonably be considered to be a municipal or school tax), lease rental or bonus of as an amount, however described, that may reasonably be regarded as being in lieu of any such amount, and that may reasonably be regarded as being in relation to

(iv) the acquisition, development or ownership of a Canadian resource property or a property that would have been a Canadian resource property if it had been acquired after 1971, or

(v) the production in Canada of

(A) petroleum, natural gas or related hydrocarbons from a mineral resource in Canada or an oil or gas well in Canada, or

(B) metal or minerals, to any stage that is not beyond the prime metal stage or its equivalent, from a mineral resource in Canada.

Situated on property in Canada in which the taxpayer had an interest with respect to which the obligation imposed by statute or the contractual obligation, as the case may be, applied

(ii) à un mandataire de Sa Majesté du chef du Canada ou d'une province, ou

(iii) à une corporation, commission ou association contrôlée directement ou indirectement, de quelque façon que ce soit, par Sa Majesté du chef du Canada ou d'une province ou par un mandataire de Sa Majesté du chef du Canada ou d'une province

À titre de redevance, de taxe (autre qu'une taxe ou fraction de taxe qui peut raisonnablement être considérée comme une taxe municipale ou scolaire), de loyer, de prime, ou à titre de somme, quelle que soit la façon dont elle est désignée, qui peut être raisonnablement considérée comme tenant lieu d'une telle somme, qui peut raisonnablement être considérée comme rattachée

(iv) à l'acquisition, à l'aménagement ou à la propriété d'un avoir minier canadien ou d'un bien qui aurait été un avoir minier Canadien s'il avait été acquis après 1971, ou

(v) à la production au Canada

(A) de pétrole, de gaz naturel ou d'hydrocarbures apparentés tirés de ressources minérales ou d'un puis de pétrole ou de gaz, ou

(B) de métaux ou de minerai, jusqu'à un stade ne dépassant pas celui du métal primaire ou de son équivalent, tirés de ressources minérales

situées au Canada sur un bien dans lequel le contribuable avait une participation assujettie à l'obligation imposée par une loi ou à l'obligation contractuelle, selon le cas;

Crown Liability and Proceedings Act, R.S.C. 1980, c. C-50

Loi sur la responsabilité civile de l'État et le contentieux administratif, L.R. 1985, ch. C-50

Interest
Prejudgment interest, cause of action outside province

31(2) A person who is entitled to an order for the payment of money in respect of a cause of action against the Crown arising outside any province or in respect of causes of action against the Crown arising in more than one province is entitled to claim and have included in the order an award of interest thereon at such rate as the court considers reasonable in the circumstances, calculated

(*a*) where the order is made on a liquidated claim, from the date or dates the cause of action or causes of action arose to the date of the order; or

(*b*) where the order is made on an unliquidated claim, from the date the person entitled gave notice in writing of the claim to the Crown to the date of the order.

Intérêt
Intérêt avant jugement — Fait non survenu dans une seule province

31(2) Dans une instance visant l'État devant le tribunal et dont le fait générateur n'est pas survenu dans une province ou dont les faits générateurs sont survenus dans plusieurs provinces, les intérêts avant jugement sont calculés au taux que le tribunal estime raisonnable dans les circonstances et :

a) s'il s'agit d'une créance liquide, depuis la ou les dates du ou des faits générateurs jusqu'à la date de l'ordonnance de paiement;

b) si la créance n'est pas liquide, depuis la date à laquelle le créancier a avisé par écrit l'État de sa demande jusqu'à la date de l'ordonnance de paiement.

Annex « B »

Syncrude Remission Order, C.R.C. , C. 794

REMISSION

3. (1) Subject to subsection (2), remission is hereby granted to each participant of any tax payable for a taxation year pursuant to Part I of the Income Tax Act as a result of the royalty provisions being applicable to

(*a*) amounts receivable and the fair market value of any property receivable by the Crown as a royalty, tax, rental or levy with respect to the Syncrude Project, or as an amount however described, that may reasonably be regarded as being in lieu of any of the preceding amounts;

Décret de remise relatif à Syncrude, C.R.C., c. 794

REMISE

3. (1) Sous réserve du paragraphe (2), remise est accordée à chaque participant de tout impôt payable pour une année d'imposition en vertu de la Partie I de la Loi de l'impôt sur le revenu et qui résulte de l'application des dispositions relatives aux redevances aux

a) montants à recevoir et à la juste valeur marchande des biens à recevoir par la Couronne à titre de redevance, d'impôt, de loyer ou de prélèvement à l'égard du projet Syncrude, ou à titre de montant, quelle que soit la manière dont il est décrit, qui peut raisonnablement être considéré comme remplaçant un des montants qui précèdent;

Annex « C »

Amendment No. 6, Schedule A-1

(formula for calculating the royalty receivable by the Alberta Crown, with respect to the Expanded Syncrude Project, excluding minimum royalty years)

$$(DP \times TR) - (AC + CP) = AS$$

Where:

DP	—	represents the Deemed Net Profit of the Alberta Joint Venture for the Syncrude Project for that period;
TR	—	represents the Transitional Rate for that period;
(DP x TR)	—	represents Alberta Royalty's unadjusted share of the Deemed Net Profit;
AC	—	represents the Annual Capital Credit for that period;
CP	—	represents the outstanding balance in the Capital Credits Pool at the end of that period; and
AS	—	represents Alberta Royalty's share of the Deemed Net Profit for that period.

FEDERAL COURT

SOLICITORS OF RECORD

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APPEARANCES:

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