Federal Court  Cour fédérale

Date: 20140902

Docket: T-1382-06

Citation: 2014 FC 838

Ottawa, Ontario, September 2, 2014

PRESENT: The Honourable Madam Justice Gagné

BETWEEN:

IMPERIAL OIL RESOURCES LIMITED

Applicant

and

THE ATTORNEY GENERAL OF CANADA

Respondent

JUDGMENT AND REASONS

Overview

[1] This is an application for judicial review brought by Imperial Oil Resources Limited [Imperial Oil] against the Attorney General of Canada, representing the Minister of National Revenue [Minister] relating to the *Syncrude Remission Order*, CRC, c 794 [SRO], an initiative undertaken in 1976 by the federal government to provide some federal tax relief to participants in the Syncrude (oil sands) project in northern Alberta. This tax relief, in the form of a remission paid

pursuant to the *Financial Administration Act*, RSC, 1985, c F-11, served to counterbalance increased royalty charges enacted by the Albertan government that, as of 1994, had to be included in the participants' taxable income. In essence, until the end of 2003, participants in the Syncrude project were entitled to a remission of federal tax for the amount they paid Alberta in royalty charges.

[2] This application was heard concurrently with files T-1-05 and T-2155-10, which deal with unpaid refund interest allegedly accrued on previously granted remission for the 1996 and 1999 taxation years. In essence, the respondent argues that no interest is owed on remission and that the application relating to the 1996 taxation year is time-barred. Reasons for those files will be addressed in a companion decision.

[3] The present file concerns the computation of the remission entitlement itself, for the 2001 taxation year. While in its Notice of Application, the applicant had also sought the corresponding claim for refund interest allegedly accrued, it desisted from that argument at the hearing.

[4] Imperial Oil submits that its remission entitlement must be imputed with reference to the actual amount of royalties payable to the Province of Alberta. The Syncrude participants (including Imperial Oil) had sought a downward adjustment to their royalties by submitting proposed financial statements to Alberta, which included deductions pertaining to certain pension costs from the 2000 and 2001 taxation years. These proposed financial statements were rejected by Alberta and ultimately by a binding arbitration decision rendered in 2004, as being inconsistent with the royalty agreement governing the computation of royalties. As such, the royalty payable was never actually

reduced by Alberta. The respondent limited Imperial Oil's remission entitlement to an amount of remission computed on the basis of the proposed lower royalties, stating that it was the amount of royalty eligible for remission.

[5] The respondent argues that the quarrel does not concern the amount of remission owed, but rather the year during which it was liable to be paid. Considering the SRO expired at the end of 2003, the respondent submits that this adjusted royalty was receivable by Alberta in 2004 following the arbitration panel's decision, so that the applicant is not entitled to the difference in remission on the amount it alleges to have actually paid in royalties and included in its 2001 taxable income. In reply, the applicant argues that the remission amount relating to the pension costs was payable in 2001, when the oil sands subjected to the royalties in question were extracted, and that it is in fact entitled to remission notwithstanding the final amount being confirmed in 2004.

[6] For the reasons discussed below, I will grant this judicial review and set aside the respondent's decision that remission is owed based on reduced royalties paid to Alberta for Imperial Oil's 2001 taxation year.

Background

[7] The relevant facts detailing Imperial Oil's business operations, participation in the Syncrude Joint Venture and the Alberta Crown Agreement, along with the historical background giving rise to the enactment of the SRO are detailed in the companion judgment. Terms used in the present reasons are, if not defined herein, as defined in the companion judgment.

[8] Through the years, the Alberta Crown Agreement was amended a number of times. The relevant amendment for this application is Amendment #6, dated January 1, 1997. Pursuant to section 2.11 (which substituted a new Clause 305 into the Alberta Crown Agreement), Alberta was entitled to a royalty equal to "Alberta's royalty's share of Deemed Net Profit" from the Syncrude Joint Venture, as calculated in accordance with Schedule A-1. As a result, Syncrude Canada was required to produce financial statements detailing the calculation of Deemed Net Profit or loss for the project and of Alberta's Deemed Net Profit or loss, including an auditor's opinion as to the reasonableness of such calculations. The annual financial statements were to be prepared in accordance with the terms and conditions set out in Schedule A-1 of Amendment #6.

[9] In December 2001, Syncrude Canada advised Alberta that the December 2000 financial statements for the determination of Alberta's share of Deemed Net Profit, previously submitted to the province, would be restated to increase allowed operating costs to recognize pension plan increased costs. Similarly, Syncrude Canada advised that the December 2001 financial statements would also be restated to recognize pension performance results. The changes in the financial statements resulted from a change in accounting treatment of future employment benefits stemming from changes to the CICA Handbook, effective January 1, 2000 [Disputed Costs].

[10] Notwithstanding the revised financial statements, the Syncrude Joint Venture participants, including Imperial Oil, remitted to Alberta, in respect of their 2001 taxation year, royalties in accordance with the original December 2001 financial statements.

[11] As a result, the Syncrude participants claimed that the royalty payments they had made to the Province of Alberta exceeded their obligations pursuant to Schedule A-1 to Amendment #6.

[12] The Province of Alberta objected to the restated financial statements, which led to the province and Syncrude Canada entering into an arbitration agreement whereby an arbitration panel [Panel] was asked to rule on whether the change in accounting treatment for future employee benefits resulting in the restated financial statements complied with the requirements of Amendment #6.

[13] On October 21, 2004, the Panel held that the restated financial statements did not comply with the requirements of Amendment #6 and, as a result, the amount of the royalty paid to Alberta was never adjusted to reflect the restated financial statements.

[14] When the Minister calculated Imperial Oil's entitlement to remission under the SRO for its 2001 taxation year, the Minister did so with reference to an amount of royalties that were reduced to Imperial Oil's share of the Disputed Costs, even though the amount of royalties paid to Alberta, and ultimately upheld as the correct amount by the Panel, was not similarly reduced.

Issues and Standard of Review

[15] This application for judicial review raises the following issue:

- Whether Imperial Oil is entitled to remission under the SRO in respect of the actual royalty paid to the Province of Alberta for its 2001 taxation year rather than

> the notional amount of royalty that would have arisen had the restated financial statements been accepted by Alberta and the Panel.

[16] The parties agree that the applicable standard of review concerning the proper interpretation of the SRO and the *Income Tax Act* (R.S.C., 1985, c. 1 (5th Supp.)) [ITA] is correctness, as it is a question of law (*Canada (Attorney General) v Imperial Oil Resources Limited*, 2009 FCA 325 [*Imperial Oil*] at para 2).

Analysis

[17] I agree with the applicant that Amendment #6 imposed an absolute liability on it to pay to Alberta its proportionate share of Alberta's share of Deemed Net Profit.

[18] The SRO grants remission of "any tax payable" as a result of the royalty provisions of the ITA being applicable to amounts receivable by Alberta as a royalty. The generally accepted definition of "receivable" is that for an amount to be considered receivable, "it is not enough that the so-called recipient have a precarious right to receive the amount in question, […] he must have a clearly legal, though not necessarily immediate, right to receive it" (*Minister of National Revenue v Colford Contracting Company Limited,* 60 DTC 1131).

[19] Amendment #6 sets out the clear and unconditional right of Alberta to receive its share of Deemed Net Profit. Imperial Oil has a corresponding obligation to pay its proportionate share of that Alberta royalty.

[20] The amount receivable by Alberta, and indeed paid by Imperial Oil, was based on the royalties paid by Imperial Oil to Alberta without any reduction in respect of the Disputed Costs.

[21] Syncrude Canada, as the operator of the Syncrude project, was required to prepare financial statements calculating the Alberta royalty. Syncrude Canada filed such financial statements for the 2000 and 2001 taxation years.

[22] The Province of Alberta accepted the original 2000 financial statements as being correctly filed. Consequently, prior to submitting the revised financial statements, both the Province of Alberta and the Syncrude Joint Venture participants agreed that the Alberta royalty, as initially calculated by Syncrude Canada, reflected the amount of the Syncrude participants' obligation to Alberta for 2000.

[23] As for 2001, although Imperial Oil filed the restated financial statements, it paid royalty without deduction of the Disputed Costs. The right to deduct those costs was subsequently submitted to arbitration.

[24] Paragraph 12(1) (*o*) of the ITA requires that any amount receivable by a province that is a royalty paid by a taxpayer must be included in income. As the amount of the Alberta royalty (without reduction for the Disputed Costs) paid by Imperial Oil is an amount receivable by Alberta as a royalty, it is required to be included in Imperial Oil's income for the taxation year during which the oil is extracted.

[25] The SRO grants remission to Imperial Oil with respect to the amount included in Imperial Oil's income pursuant to paragraph 12(1)(*o*) of the ITA. Consequently, Imperial Oil is entitled to remission on its full share of the Alberta royalty paid without reduction in respect of the Disputed Costs.

[26] The respondent suggests that such portion was a contingent liability that did not crystallize as a liability of Imperial Oil until 2004, when the Panel released its decision concluding that Alberta's share of Deemed Net Profit could not be reduced by the Disputed Costs.

[27] The Supreme Court of Canada in *Her Majesty the Queen v McLarty*, [2008] 2 SCR 79, stated, in determining whether a liability is a contingent liability, that "[t]he test is simply whether a legal obligation comes into existence at a point in time or whether it will not come into existence until the occurrence of an event which may never occur."

[28] Imperial Oil's obligation to pay its proportionate share of the Alberta royalty came into existence pursuant to Amendment #6 and was not dependent on the occurrence of an event which may never have occurred. In particular, clause 305 of the Amendment #6 specifically says that the Province of Alberta is entitled to its share of Deemed Net Profit "for each period" (which is defined in Schedule A-1 to be a year). Therefore, the liability arises in respect of each particular year. The simple fact that its exact quantum be determined later does not impact the prior existence of the obligation.

[29] Moreover, a conclusion that the portion of the Alberta royalty relating to the Disputed Costs only became receivable in 2004 (when the Panel made its decision) would be contrary to the very nature of the royalty imposed by Amendment #6. As the Federal Court of Appeal noted in *Imperial Oil*, the essential nature of a royalty is necessarily linked to the production from a particular property. In this case, the royalty obligation imposed by Amendment #6 is with respect to the particular property that was produced in 2001.

[30] Therefore, the Court's finding would be the same even if Imperial Oil would have deducted the Disputed Costs from the Alberta royalty paid in 2001 and would have subsequently been forced to pay the difference in 2004, once the Panel decision was rendered.

[31] In other words, the Panel's decision simply interprets Syncrude Canada and Alberta's rights pursuant to Amendment #6; it is not a *constitutive-investitive* or a *divestive* decision which, by its nature, can create a new legal relationship between the parties.

* * *

[32] It is uncontested that the amount of royalty paid to Alberta in 2001 included the Disputed Costs. However, the parties vigorously disagree and, I would say, they both remained vague during the hearing as to whether they were included in Imperial Oil's income for its 2001 taxation year. As the SRO allows the Minister to grant remission on amounts included in the producer's income pursuant to paragraph 12(1) (*o*) of the ITA (not only paid in royalty), this question is somewhat crucial.

[33] The respondent initially claimed that only $41.9 million was included in Imperial Oil's income for 2001, and that the Disputed Costs were not included in that amount, as $43 million were paid to Alberta. However, Mr. Ladak from the Canada Revenue Agency [CRA], conceded during his cross-examination that it was rather an amount of $54 million that was included in Imperial Oil's 2001 revenue for the Syncrude royalty pursuant to paragraph 12(1)(*o*) of the ITA. However, the respondent maintains that the Disputed Costs are not included in the $54 million and that the excess of $54 million over $41.9 million concerns other amounts disputed before the Appeals division of the CRA.

[34] Just as firmly, Imperial Oil argues that it is not relevant whether or not the Disputed Costs were included in Imperial Oil's revenue and that the only question that should be of concern to the Court is whether or not at least $43 million were included in Imperial Oil's taxable income, as it is only asking for remission of tax paid on $43 million.

[35] Imperial Oil cites the Federal Court of Appeal's decision in *Imperial Oil* for the proposition that the Syncrude royalty can not be broken down or "chip chopped". Asking ourselves if the Disputed Costs were included or not in its 2001 revenue under 12(1) (*o*) of the ITA, says Imperial Oil, would only amount to breaking down the Syncrude royalty. This argument, which was successfully made by the respondent in *Imperial Oil*, supports, as indicated above, Imperial Oil's position that the Syncrude royalty remains intimately linked with the oil extracted in a given year, even if the exact amount of the royalty is determined by an arbitration decision rendered during a different year. However it does not support Imperial Oil's argument

that one should not, without breaking down the royalty, ask oneself if the Disputed Costs were included in Imperial Oil's revenue for its 2001 taxation year.

[36] Imperial Oil's argument simply contradicts the terms of the SRO. The SRO dictates that an amount has to be included in the producer's taxable revenue, and tax paid on that amount, in order for that amount of tax to be remitted.

[37] The Court is asked to review the decision of the Minister concerning the Disputed Costs and is not asked to rule on any other amount that would need to be reassessed by the CRA, so that the amount of Syncrude royalty included in Imperial Oil's taxable revenue for the 2001 taxation year ($54 million) equates the taxable amount used to calculate the remission for the same year ($41.9 million).

[38] Although the Court has been presented the above general figures, it does not have the benefit of Imperial Oil's entire tax file and of the documentation supporting these figures. The evidence before the Court is incomplete and contradictory as to whether or not the Disputed Costs were included in Imperial Oil's revenue.

[39] In any event, I am of the opinion that this question is for the CRA (who has the benefit of Imperial Oil's tax file), and eventually the Tax Court, to answer.

Conclusion

[40] For these reasons, the Court will grant the application for judicial review, set aside the Minister's decision and declare that the applicant's entitlement to relief for the 2001 taxation year pursuant to the SRO, without a deduction related to the Disputed Costs, is contingent upon the Disputed Costs having been included in Imperial Oil's 2001 taxable income.

JUDGMENT

THIS COURT'S JUDGMENT is that:

1. The application for judicial review is granted;
2. The decision of the Minister of National Revenue first communicated to the applicant by way of a Notice of Reassessment dated July 17, 2006 in respect of the 2001 taxation year deducting the Disputed Costs from the calculation of the relief available to the applicant under the terms of the Syncrude Remission Order, is set aside;
3. The Court declares that, to the extent that the Disputed Costs were included in the applicant's taxable income for the 2001 taxation year, the applicant is entitled to relief for the 2001 taxation year, pursuant to the Syncrude Remission Order, without deduction related to the Disputed Costs;
4. The file is remitted back to the Minister of National Revenue for re-determination in accordance with the present reasons; and
5. Costs are granted in favour of the applicant.

"Jocelyne Gagné"

Judge

FEDERAL COURT

SOLICITORS OF RECORD

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