Docket: 2002-2640(IT)G

BETWEEN:

COGEMA RESOURCES INC., (THE SUCCESSOR CORPORATION OF 3326110 CANADA LTD., FORMERLY CORONA GRANDE EXPLORATION CORPORATION),

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeals of *Cogema Resources Inc.* (2002-3762(IT)G and 2002-4062(IT)G) on November 1, 2004 at Saskatoon, Saskatchewan

By: The Honourable Justice D.W. Beaubier

Appearances:

Counsel for the Appellant:	Kurt Wintermute
Counsel for the Respondent:	Gerald Chartier

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 1994, 1995 and 1996 taxation years are allowed and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

The Appellant is awarded its party-and-party costs, but only one set of costs is to be taxed respecting the hearing.

Signed at Ottawa, Canada, this 9th day of November 2004.

Beaubier, J.

Docket: 2002-3762(IT)G

BETWEEN:

COGEMA RESOURCES INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeals of *Cogema Resources Inc., (The Successor Corporation of 3326110 Canada Ltd., formerly Corona Grande Exploration Corporation)* (2002-2640(IT)G) and *Cogema Resources Inc.* (2002-4062(IT)G) on November 1, 2004 at Saskatoon, Saskatchewan

By: The Honourable Justice D.W. Beaubier

Appearances:

Counsel for the Appellant:	Kurt Wintermute
Counsel for the Respondent:	Gerald Chartier

JUDGMENT

The appeals from the reassessments made under the *Income Tax Act* for the 1994 and 1995 taxation years are allowed and the reassessments are referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

The Appellant is awarded its party-and-party costs, but only one set of

costs is to be taxed respecting the hearing.

Signed at Ottawa, Canada, this 9th day of November 2004.

Beaubier, J.

Docket: 2002-4062(IT)G

BETWEEN:

COGEMA RESOURCES INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeal heard on common evidence with the appeals of *Cogema Resources Inc., (The Successor Corporation of 3326110 Canada Ltd., formerly Corona Grande Exploration Corporation)* (2002-2640(IT)G) and *Cogema Resources Inc.* (2002-3762(IT)G) on November 1, 2004 at Saskatoon, Saskatchewan

By: The Honourable Justice D.W. Beaubier

Appearances:

Counsel for the Appellant: Kurt Wintermute

Counsel for the Respondent: Gerald Chartier

JUDGMENT

The appeal from the reassessment made under the *Income Tax Act* for the 1996 taxation year is allowed and the reassessment is referred back to the Minister of National Revenue for reconsideration and reassessment in accordance with the attached Reasons for Judgment.

The Appellant is awarded its party-and-party costs, but only one set of

costs is to be taxed respecting the hearing.

Signed at Ottawa, Canada, this 9th day of November 2004.

Beaubier, J.

Citation: 2004TCC750
Date: 20041109
Docket: 2002-2640(IT)G

BETWEEN:
COGEMA RESOURCES INC., (THE SUCCESSOR CORPORATION OF 3326110 CANADA LTD., FORMERLY CORONA GRANDE EXPLORATION CORPORATION),

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent,

Docket: 2002-3762(IT)G
2002-4062(IT)G

BETWEEN:
COGEMA RESOURCES INC.,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

REASONS FOR JUDGMENT

Beaubier,J.

[1] These appeals for the years 1994, 1995 and 1996 were heard together on common evidence at Saskatoon, Saskatchewan on November 1, 2004. The Appellant called its Senior Vice President and Financial Officer, Gerald Sherman, C.A. and read in part of the examination for discovery of the Respondent's auditor

in the files, Patrick Robert Saint Pierre. Respondent's counsel filed various documents without objection by the Appellant.

[2] At the outset of the hearing the parties filed Exhibit AR-1 agreeing to judgment on all except one issue. Those matters are determined accordingly. It reads:

ISSUES CONCEDED BY THE RESPONDENT

2002-2640(IT)G

Cogema Resources Inc. (the successor corporation of 3326110 Canada Ltd., formerly Corona Grande Exploration) v. The Minister of National Revenue

1. With respect to the 1994 taxation year of the Appellant, allow a deduction to the Cluff Mining Partnership for the rent paid under the Current Surface Lease in the amount of $528,179.25 as a properly deductible expense in 1994, resulting in a decrease to the partnership income of the Appellants predecessor corporation, Corona Grande Exploration Corporation, in the amount of $105,635.00.

2. With respect to the 1995 taxation year of the Appellant, allow a deduction to the Cluff Mining Partnership for the rent paid under the Current Surface Lease in the amount of $528,179.25 as a properly deductible expense in 1995, resulting in a decrease to the partnership income of the Appellants predecessor corporation, Corona Grande Exploration Corporation, in the amount of $105,635.00.

3. With respect to the 1996 taxation year of the Appellant, allow a deduction to the Cluff Mining Partnership for the rent paid under the Current Surface Lease in the amount of $504,300.25 as a properly deductible expense in 1996, resulting in a decrease to the partnership income of the Appellants predecessor corporation, Corona Grande Exploration Corporation, in the amount of $100,860.05.

2002-3762(IT)G

Cogema Resources Inc. v. The Minister of National Revenue

1. With respect to the 1994 taxation year of the Appellant, allow a deduction for additional interest in the amount of $28,005.00 as a properly deductible expense in 1994.

2. With respect to the 1994 taxation year of the Appellant allow a deduction for rent paid in the amount of $528,179.00 as a properly deductible expense in 1994, resulting in the decrease in partnership income of the Appellant in the amount of $422,543.00.

3. With respect to the 1995 taxation year of the Appellant, allow a deduction for interest in the amount of $104,269.00 as a properly deductible expense in 1995.

4. With respect to the 1995 taxation year of the Appellant, allow a deduction to the Cluff Mining Partnership for rent paid in the amount of $528,179.00 as a properly deductible expense in 1995, resulting in a decrease in the partnership income of the Appellant in the amount of $422,543.00.

2002-4062(IT)G

Cogema Resources Inc. v. The Minister of National Revenue

1. With respect to the 1996 taxation year of the Appellant, allow a deduction for an interest expense in the amount of $979,901.00.

2. With respect to the 1996 taxation year of the Appellant, allow a deduction to the Cluff Mining Partnership for rent paid in the amount of $504,300.00 as a properly deductible expense in 1996, resulting in a decrease in the partnership income of the Appellant in the amount of $403,440.00

[3] The Appellant ("Cogema") mined uranium ore in Saskatchewan. It deducted a resources surcharge which it paid respecting uranium yellowcake (U_3O_8) under *The Corporation Capital Tax Act (Saskatchewan)*, S.S. 1979-80 c. C-38.1 (the "*Saskatchewan Act*"). The central issue at the hearing which remained in dispute is whether that surcharge was a tax paid in relation to production in Canada of a mineral resource located in Canada and whether its deduction is denied under paragraph 18(1)(*m*) of the *Income Tax Act*.

[4] Subparagraph 18(1)(*m*)(v)(B) of the *Income Tax Act* for 1994 – 1996 reads:

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

(iii) a corporation, commission or association that is controlled 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 of a tax 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 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

(v) the production in Canada of …

(B) metal, minerals (other than iron or petroleum or related hydrocarbons) or coal from a mineral resource in Canada to any stage that is not beyond the prime metal stage or its equivalent, …

[5] The deductions claimed by Cogema for surcharges paid under the *Saskatchewan Act* were:

1994 $2,020,888

1995	$1,612,637
1996	$1,879,699

They were paid pursuant to section 13.1 of the *Saskatchewan Act*, which in those years read in part:

> 13.1 In addition to any tax payable pursuant to subsection 13(1), a resource corporation shall, with respect to each of its fiscal years, pay a tax in an amount equal to the positive difference between:
>
> (a) the aggregate of: …
>
> (iii) if a fiscal year or portion of a fiscal year commences on or after April 1, 1993, 3.6% of the resource corporation's value of resource sales in that fiscal year or portion of that fiscal year; and
>
> (b) the tax payable, if any, by the resource corporation pursuant to this Act determined in accordance with subsection 13(1) for the corresponding fiscal year mentioned in clause (a).

[6] The surcharge was not paid at the time of production of the ore or of the yellowcake. It was paid at the time of sale of that yellowcake. Two problems were raised as to these sales.

The first was that in 1995 Cogema sold yellowcake that it had swapped and received from Denison. Mr. Sherman "believed" that Denison's yellowcake was not all mined in Saskatchewan. "Belief" is not knowledge and "belief" is not enough to refute the Respondent's assumptions that all of the ore in question was from the Cluff Lake mine in Saskatchewan which was leased from Saskatchewan. Mr. Sherman's belief was stated frankly and honestly.

[7] The second problem raised was that section 13.1 of the *Saskatchewan Act* levies the surcharge on resource sales, which at that time was taken by Saskatchewan to mean the definition of "gross sales" in Part III of *The Crown Mineral Royalty Schedule*, 1986, pursuant to *The Mineral Disposition Regulations 1986*. It reads:

> 15(1)(n) "gross sales" means the aggregate of the sales prices and all other amounts paid or payable to or for the benefit of the

> royalty payer for uranium ore or uranium concentrate produced from the Crown lease, and in computing gross sales the rules set out in section 19 shall apply;

As an aside, for the purposes of the issue in dispute, sections 19 and 32 of the *Regulations* cause the surcharge on the swap to be levied at the time that Cogema sells the swapped material, even if it was produced outside of Canada. Failing those provisions, this Court would find the sale of the swapped material to have occurred when Cogema transferred it to Denison. Therefore, Regulations 19 and 32 postpone the levying of the surcharge.

[8] Paragraph 18(1)(*m*) of the *Income Tax Act* forbids a deduction of … an amount paid … (to Saskatchewan) as a royalty, tax … that may reasonably be regarded as being in relation to … (v) the production in Canada of … (B) … minerals ….

[9] The evidence is that produced and inventoried ore or yellowcake is not subject to the surcharge; rather, the surcharge is levied at its sale. For this reason, the Appellant argues, in essence, that the surcharge is a sales tax and therefore is deductible. To forbid the deduction of the surcharge, 18(1)(*m*) should have referred to "the proceeds realized from the sale or disposition of production."

[10] The Respondent's argument concedes that the surcharge is not levied on the annual production as the yellowcake is produced by Cogema. Rather the surcharge occurs when the conditions of section 13.1 of the *Saskatchewan Act* apply. In essence, the value of production for surcharge purposes is established at the time of sale as specified in the *Saskatchewan Act*.

[11] Respecting paragraph 18(1)(*m*) of the *Income Tax Act*, Sharlow J.A., speaking for the Federal Court of Appeal, stated at paragraphs 20 to 25 inclusive of *Mobil Oil Canada Ltd. v. R*, 2001 DTC 5668:

> [20] In my view, Mobil's proposed definition incorrectly assumes that the word "royalty" as used in paragraph 18(1)(m) is limited to its meaning in the commercial context. It must be borne in mind that paragraph 18(1)(m) deals fundamentally with payments to the Crown. It is therefore appropriate to recall that the word "royalty" in its original sense refers to Crown prerogatives or Crown rights. That meaning of "royalty" was applied in *Attorney-General of Ontario v. Mercer* (1883), 8 App. Cas. 767 (P.C.) to the interpretation of section 109 of what is now the *Constitution Act*, 1867, which reads as follows:

All Lands, Mines, Minerals, and Royalties belonging to the several Provinces of Canada, Nova Scotia, and New Brunswick at the Union, and all Sums then due or payable for such Lands, Mines, Minerals, or Royalties, shall belong to the several Provinces of Ontario, Quebec, Nova Scotia, and New Brunswick in which the same are situate or arise, subject to any Trusts existing in respect thereof, and to any Interest other than that of the Province in the same.	Toutes les terres, mines, minéraux et réserves royales appartenant aux différentes provinces du Canada, de la Nouvelle-Écosse et du Nouveau-Brunswick lors de l'union, et toutes les sommes d'argent alors dues ou payables pour ces terres, mines, minéraux et réserves royales, appartiendront aux différentes provinces d'Ontario, Québec, la Nouvelle-Écosse et le Nouveau-Brunswick, dans lesquelles ils sont sis et situés, ou exigibles, restant toujours soumis aux charges dont ils sont grevés, ainsi qu'à tous intérêts autres que ceux que peut y avoir la province.

[21] The word "royalty" is still used in Canada to describe a payment that is required by a provincial statute to be paid to the province as a share of the production of a resource. Typically, in the case of a resource that the province owns, there is a provincial statute that authorizes the granting of a lease subject to the payment of royalties. The Saskatchewan *Mineral Resources Act*, R.S.S. 1978, c. M-16 is an example of such a statute. However, there is no authority that suggests that the word "royalty" must be limited to amounts paid pursuant to such an arrangement. In the context of payments to a province, the word "royalty" may describe any share of resource production that is paid to the province in connection with its interest in the resource.

[22] Under the *Road Allowances Crown Oil Act*, Mobil had the right to sell its entire oil production for the years under appeal, including the Province's 1.88% share, upon paying the Province an amount equal to 1% of the total value of the production. In my view, that 1% payment is a royalty even though it was the *Road*

> *Allowance Crown Oil Act* itself that created the Province's 1.88% proprietary interest. I conclude, therefore, that the payments in question are "royalties" within the meaning of paragraph 18(1)(m) of the *Income Tax Act*.
>
> *Second condition: To what do the payments relate?*
>
> [23] With respect to the second condition, it is necessary to consider only subparagraph 18(1)(m)(v). In support of its position that the payments are not within the scope of subparagraph 18(1)(m)(v), Mobil argues that the payments represent the Province's net share of its 1.88% ownership in the oil produced, and that Mobil had no rights in respect of the Crown's 1.88% share.
>
> [24] I do not read subparagraph 18(1)(m)(v) as imposing any condition as to the ownership of the oil with respect to which the payments were made. In my view only two questions need be asked. The first question is whether Mobil had the right to take or remove the oil from the property. The answer to that question must be yes. Mobil owned the leases that were the legal source of its right to take or remove the oil. The fact that the production of the oil triggered certain obligations under the *Road Allowances Crown Oil Act* did not derogate from Mobil's right under the leases to take or remove the oil. The second question is whether the payments may reasonably be considered to relate to the exercise of Mobil's right to remove the oil from the ground. The answer to that question must also be yes. Section 4 of the *Road Allowances Crown Oil Act* expressly ties the exercise of that right to the obligation to make the payments. It follows that the payments are within the scope of subparagraph 18(1)(m)(v).
>
> *Conclusion*
>
> [25] The Trial Judge correctly concluded that in computing Mobil's income for 1977, 1978, 1979 and 1980 under the *Income Tax Act*, paragraph 18(1)(m) prohibits the deduction of the payments made to the Province of Saskatchewan pursuant to section 4 of the *Road Allowances Crown Oil Act*. These appeals should be dismissed with costs.

[12] Ultimately, the following question arises respecting the surcharge:

> Would the surcharge be levied on the Appellant if the yellowcake was not sold by the Appellant and instead, the yellowcake was used by the

> Appellant to manufacture a product such as uranium fuel rods which it then used itself?

[13] Under 15(1)(*n*) (see paragraph [7]) the answer is:

> No.

There would be no sales prices … paid… to … the royalty payer for uranium or uranium concentrate.

[14] The answer "No" would remain correct even if the uranium fuel rods were not beyond the prime metal stage or its equivalent (subparagraph 18(1)(*n*)(v)(B)), because under the *Saskatchewan Act* and *Regulations*, they must be sold for the surcharge to be levied.

[15] In other words, the second question answered by Sharlow, J.A. in paragraph [24] of *Mobil* must be answered "No" because the surcharge related to Cogema's actual sale of the mineral and not its right to remove the mineral from the ground. The surcharge was a sales tax and was in relation to the sale of minerals, not the production of minerals.

[16] The appeals are allowed and these matters are referred back to the Minister of National Revenue for reconsideration and reassessment pursuant to these Reasons.

[17] The Appellant is awarded its party-and-party costs, but only one set of costs is to be taxed respecting the hearing.

Signed at Ottawa, Canada this 9th day of November 2004.

"D.W. Beaubier"

Beaubier, J.

CITATION:	2004TCC750
COURT FILE NOS.:	2002-2640(IT)G, 2002-4062(IT)G, 2002-3762(IT)G
STYLE OF CAUSE:	Cogema Resources Inc. v. The Queen
PLACE OF HEARING:	Saskatoon, Saskatchewan
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REASONS FOR JUDGMENT BY:	The Honourable Justice Beaubier
DATE OF JUDGMENT:	November 9, 2004

APPEARANCES:

Counsel for the Appellant:	Kurt Wintermute
Counsel for the Respondent:	Gerald Chartier

COUNSEL OF RECORD:

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