Docket: 2004-1650(IT)G,

BETWEEN:

GARRET MADELL,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

Appeals heard on June 11, 12 and 13, 2007 at Calgary, Alberta, August 3, 2007 by way of conference call at Vancouver, British Columbia and September 19, 2007, at Edmonton, Alberta

Before: The Honourable Justice L.M. Little

Appearances:

Counsel for the Appellant:	James G. Shea and Matt Clark
Counsel for the Respondent:	John O'Callaghan and Chang Du

JUDGMENT

The appeals from the assessments made under the *Income Tax Act* for the 1997 and 1998 taxation years are dismissed, with costs, in accordance with the attached Reasons for Judgment.

Signed at Toronto, Ontario, this 2nd day of May 2008.

"L.M. Little"

Little J.

Citation: 2008TCC264
Date: 20080502
Docket: 2004-1650(IT)G

BETWEEN:

GARRET MADELL,

Appellant,

and

HER MAJESTY THE QUEEN,

Respondent.

<u>REASONS FOR JUDGMENT</u>

<u>Little J.</u>

A. <u>Facts</u>

[1] The Appellant is an individual who resides in the city of Calgary, Alberta.

[2] The Appellant's appeal and the appeals filed by Messrs. Storwick, Falkenberg, and Caputo were heard on common evidence.

[3] The four Appellants were "test cases" for approximately 460 investors.

[4] The four Appellants were proceeding as Representative Appeals on behalf of the other investors who have filed Notices of Objection against the Reassessments issued by the Minister of National Revenue (the "Minister").

[5] In 1997 the Appellant purchased 10 limited partnership units in Stellar Dynamic Limited Partnership (the "Partnership"). The subscription price paid by the Appellant was $10,850 per limited partnership unit.

[6] Manhattan Ventures Ltd. ("Manhattan"), a corporation resident in Canada, was the General Partner of the Partnership.

[7] The Revised Notice of Appeal filed by the Appellant maintains that the business of the Partnership was to purchase and actively promote the Quest Prestige Card in its acquired territories and to purchase Class "A" common shares in Imaging Dynamic Corporation ("IDC"), a corporation publicly traded on the Alberta Stock Exchange.

[8] In 1997 Manhattan entered into a joint venture agreement with IDC, the object of which was to develop the IDC Digital Radiography System Engineering Prototype and share in gross revenues and expenses. Manhattan contributed $320,000[1] to the joint venture entitling it to 3.2% of the future cashflow.

[9] In 1998 Manhattan terminated the joint venture by exchanging its interest for 640,000 Class "A" shares of IDC. The full $320,000 investment was expensed and Manhattan allocated the shares and the resulting loss to the partners of the Partnership.

[10] The Quest Prestige Card was a customer loyalty card that entitled the holder to discounts at hotels, restaurants and other commercial establishments.

[11] Rockhaven International Inc. ("Rockhaven") was a company incorporated in the British Virgin Islands. Rockhaven owned the copyright to the Quest Prestige Card.

[12] Stellar Financial Services Inc. ("Stellar") was a corporation resident in Canada.

[13] Stellar and Rockhaven entered into a Distribution Agreement in 1996. Under the Distribution Agreement Stellar was required to identify territories in Canada and the United States of America in which the Quest Prestige Cards could be sold. Stellar was also to receive a commission of $1,750 for each territory sold to investors, such as the Appellant and the Partnership.

[14] In 1997 and 1998 the Partnership entered into 56 Licence Agreements with Rockhaven. The Appellant also entered into three Licence Agreements directly with Rockhaven. Pursuant to these agreements, Rockhaven granted both the

[1] Joint book of documents Vol. II tab 7.

Appellant and the Partnership the exclusive right to publish, reproduce, market and distribute the Quest Prestige Card within the territories specified in the agreements.

[15] Pursuant to the Licence Agreements, the Appellant and the Partnership agreed to pay a licence fee of $350 plus Advanced Royalties of $20,000 for each territory.

[16] Both also agreed to pay a royalty amount of $5 for each Quest Prestige Card sold, distributed, marketed, published or reproduced during the 20-year term, after the sale of the first 4,000 cards or the first year – whichever came first.

[17] The Appellant and the Partnership entered into separate Operating Agreements with Crusader Marketing Corporation Inc. ("Crusader"). The agreements provided that Crusader was retained to market and distribute the Quest Prestige Card in the territories acquired.

[18] Crusader agreed to provide cash performance bonds in the amount of $15,000 per territory. It was specified that $3 would be released to Crusader upon the sale of a Quest Prestige Card. At the expiration of the agreement the balance of the bond was to be forfeited to the Appellant and the Partnership, respectively, as damages for lack of performance.

[19] Based on the evidence presented at trial the Appellant could not confirm whether the performance bonds were actually established.

[20] When the Appellant filed his income tax returns for the 1997 and 1998 taxation years he deducted the following amounts:

	1997	1998
Limited Partnership Losses disallowed	$ 80,750	$ 55,677
Prepaid royalty expense disallowed	$ 85,038	
Licence expenses disallowed	$ 1,488	
	$167,276	$ 55,677

[21] By Notices of Reassessment dated March 13, 2000 the amounts referred to in paragraph [20] above were disallowed by the Minister.

[22] After the Notices of Reassessment were confirmed by the Minister the Appellant filed Notices of Appeal to the Tax Court of Canada.

B. Issues

[23] (a) Were the investments made by the Appellant and the Partnership to become a Quest Prestige Card distributor, a source of income for the purposes of section 9 of the *Income Tax Act* (the "*Act*")? If not, no expenses related to those investments are deductible.

(b) In the alternative, are the Advance Royalties "tax shelter investments" as defined in section 143.2 of the *Act*? If so, subsection 143.2(6) prohibits the deduction of the Advance Royalties in the years under appeal.

(c) In the further alternative, can any portion of the Advance Royalty expenses reasonably be regarded as having been made or incurred in respect of a period after the end of the years under appeal? If so, subsection 18(9) of the *Act* prohibits the deduction of the Advance Royalties in the years under appeal.

(d) In the further alternative, must the Advance Royalty expenses be matched to revenue from sales of Quest Prestige Cards when determining profit under section 9 of the *Act*? If so, no amounts in respect of the Advance Royalties are deductible in the years under appeal.

(e) In the further alternative, was any portion of the unpaid $15,000 balance of Advance Royalties, due under each Licence Agreement, a contingent liability in the years under appeal? If so, paragraph 18(1)(e) of the *Act* prohibits the deduction of the contingent amounts.

(f) In the further alternative, were the Licence Fees capital expenses? If so, paragraph 18(1)(b) prohibits their deduction as a current expense.

(g) Was the Partnership, and in return the Appellant, entitled to any deduction in respect of the IDC joint venture in determining its section 96 partnership losses?

C. Analysis and Decision

[24] As noted above, both the Appellant and the Partnership agreed to pay Rockhaven $20,350 for each territory covered by the Licence Agreement. This

payment consisted of a $20,000 Advance Royalty payment and a Licence Fee in the amount of $350.

[25] The evidence presented to the Court indicated the following:

(A) Both the Appellant and the Partnership claimed a deduction for the full amount of $20,350 per territory. However, both admitted that they never paid nor were they ever asked to pay the Advance Royalty of $15,000 per territory. In summary, the total cash outlay, per territory, was limited to $5,350.

(B) The Appellant admitted that at the time of the initial investment there was no activity by Crusader to sell Quest Prestige Cards in the territories acquired by him or the Partnership.

(C) Crusader generated no revenue from the sale of the Quest Prestige Cards in 1997. It was admitted, however that Crusader did generate nominal revenue in 1998 and 1999.

(D) The Appellant agreed that he did not conduct any investigation (either directly or indirectly) concerning the various corporate entities behind the Quest Prestige Card, before he made his investment.

(E) The Appellant agreed that he did not monitor the marketing activities of Crusader.

(F) The Appellant claimed Partnership losses on the basis that the Partnership was engaged in a joint venture agreement with IDC.

[26] In summary, neither the Appellant nor any of the other three Appellants could point to any personal activity, on their part or the part of the Partnership, of marketing the Quest Prestige Card.

[27] I will now deal with the specific issues under appeal.

I. Source of Income

[28] Counsel for the Respondent maintained that neither the Partnership nor the Appellant was engaged in a commercial activity when investments were made in the Quest Prestige Card promotion. Counsel for the Respondent also maintained

that there was no source of business or property income from which to deduct the $20,000 Advance Royalty and the $350 Licence Fee.

[29] Counsel for the Appellant and Counsel for the Respondent each referred to the decision of the Supreme Court of Canada in *Stewart v. Canada,* 2002 SCC 46 and *Walls v. Canada*, 2002 SCC 47. In *Stewart* the Supreme Court stated the following:

> 50 It is clear that in order to apply s. 9, the taxpayer must first determine whether he or she has a source of either business or property income. As has been pointed out, a commercial activity which falls short of being a business, may nevertheless be a source of property income. **As well, it is clear that some taxpayer endeavours are neither businesses, nor sources of property income, but are mere personal activities.** As such, the following two-stage approach with respect to the source question can be employed:
>
> > (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?
>
> **The first stage of the test assesses the general question of whether or not a source of income exists**; the second stage categorizes the source as either business or property.
>
> 51 Equating "source of income" with an activity undertaken "in pursuit of profit" accords with the traditional common law definition of "business", i.e., "anything which occupies the time and attention and labour of a man for the purpose of profit": *Smith*, *supra*, at p. 258; *Terminal Dock*, *supra*. As well, **business income is generally distinguished from property income on the basis that a business requires an additional level of taxpayer activity:** see Krishna, *supra*, at p. 240. As such, it is logical to conclude that an activity undertaken in pursuit of profit, regardless of the level of taxpayer activity, will be either a business or property source of income.
>
> 52 **The purpose of this first stage of the test is simply to distinguish between commercial and personal activities**, and, as discussed above, it has been pointed out that this may well have been the original intention of Dickson J.'s reference to "reasonable expectation of profit" in Moldowan. **Viewed in this light, the criteria listed by Dickson J. are an attempt to provide an objective list of factors for determining whether the activity in question is of a commercial or personal nature.** These factors are what Bowman J.T.C.C. has referred to as "indicia of commerciality" or "badges of trade": Nichol, supra, at p. 1218. **Thus, where the nature of a taxpayer's venture contains elements which suggest that it could be considered a hobby or other personal pursuit, but the venture is undertaken in a sufficiently**

> **commercial manner, the venture will be considered a source of income for the purposes of the Act.**
>
> 53 **We emphasize that this "pursuit of profit" source test will only require analysis in situations where there is some personal or hobby element to the activity in question.** With respect, in our view, courts have erred in the past in applying the REOP test to activities, such as law practices and restaurants, where there exists no such personal element: see, for example, Landry, supra, Sirois, supra, *Engler v. R.* (1994), 94 D.T.C. 6280 (Fed. T.D.). Where the nature of an activity is clearly commercial, there is no need to analyze the taxpayer's business decisions. Such endeavours necessarily involve the pursuit of profit. As such, a source of income by definition exists, and there is no need to take the inquiry any further.

(Emphasis added)

> 54 It should also be noted that the source of income assessment is not a purely subjective inquiry. Although in order for an activity to be classified as commercial in nature, the taxpayer must have the subjective intention to profit, in addition, as stated in *Moldowan*, this determination should be made by looking at a variety of objective factors. Thus, in expanded form, the first stage of the above test can be restated as follows: “Does the taxpayer intend to carry on an activity for profit and is there evidence to support that intention?” This requires the taxpayer to establish that his or her predominant intention is to make a profit from the activity and that the activity has been carried out in accordance with objective standards of businesslike behaviour.
>
> 55 The objective factors listed by Dickson J. in *Moldowan*, at p. 486, were: (1) the profit and loss experience in past years; (2) the taxpayer’s training; (3) the taxpayer’s intended course of action; and (4) the capability of the venture to show a profit. As we conclude below, it is not necessary for the purposes of this appeal to expand on this list of factors. As such, we decline to do so; however, we would reiterate Dickson J.’s caution that this list is not intended to be exhaustive, and that the factors will differ with the nature and extent of the undertaking. We would also emphasize that although the reasonable expectation of profit is a factor to be considered at this stage, it is not the only factor, nor is it conclusive. The overall assessment to be made is whether or not the taxpayer is carrying on the activity in a commercial manner. However, this assessment should not be used to second-guess the business judgment of the taxpayer. It is the commercial nature of the taxpayer’s activity which must be evaluated, not his or her business acumen.
>
> 56 In addition to restricting the source test to activities which contain a personal element, the activity which the taxpayer claims constitutes a source of income must be distinguished from particular deductions that the taxpayer associates with that source. An attempt by the taxpayer to deduct what is essentially a personal expense does not influence the characterization of the

source to which that deduction relates. This analytical separation is mandated by the structure of the Act. While, as discussed above, s. 9 is the provision of the Act where the basic distinction is drawn between personal and commercial activity, and then, within the commercial sphere, between business and property sources, the characterization of deductions occurs elsewhere. In particular, s. 18(1)(*a*) requires that deductions be attributed to a particular business or property source, and s. 18(1)(*h*) specifically disallows the deduction of personal or living expenses of the taxpayer:

> **18.** (1) In computing the income of a taxpayer from a business or property no deduction shall be made in respect of
>
> (*a*) an outlay or expense except to the extent that it was made or incurred by the taxpayer for the purpose of gaining or producing income from the business or property;
>
> ...
>
> (*h*) personal or living expenses of the taxpayer ....

57 It is clear from these provisions that the deductibility of expenses presupposes the existence of a source of income, and thus should not be confused with the preliminary source inquiry. If the deductibility of a particular expense is in question, then it is not the existence of a source of income which ought to be questioned, but the relationship between that expense and the source to which it is purported to relate. The fact that an expense is found to be a personal or living expense does not affect the characterization of the source of income to which the taxpayer attempts to allocate the expense, it simply means that the expense cannot be attributed to the source of income in question. As well, if, in the circumstances, the expense is unreasonable in relation to the source of income, then s. 67 of the Act provides a mechanism to reduce or eliminate the amount of the expense. Again, however, excessive or unreasonable expenses have no bearing on the characterization of a particular activity as a source of income.

…

60 In summary, the issue of whether or not a taxpayer has a source of income is to be determined by looking at the commerciality of the activity in question. Where the activity contains no personal element and is clearly commercial, no further inquiry is necessary. Where the activity could be classified as a personal pursuit, then it must be determined whether or not the activity is being carried on in a sufficiently commercial manner to constitute a source of income. However, to deny the deduction of losses on the simple ground that the losses signify that no business (or property) source exists is contrary to the words and scheme of the Act. Whether or not a business exists is a separate question from the deductibility of expenses. As suggested by the appellant, to disallow deductions based on a reasonable expectation of profit analysis would amount to a case law stop-loss

> rule which would be contrary to established principles of interpretation, mentioned above, which are applicable to the Act. As well, unlike many statutory stop-loss rules, once deductions are disallowed under the REOP test, the taxpayer cannot carry forward such losses to apply to future income in the event the activity becomes profitable. As stated by Bowman J.T.C.C. in *Bélec*, *supra*, at p. 123: "It would be ... unacceptable to permit the Minister [to say] to the taxpayer 'The fact that you lost money ... proves that you did not have a reasonable expectation of profit, but as soon as you earn some money, it proves that you now have such an expectation.'"

[30] I believe that the approach outlined by the Supreme Court in *Stewart* may be summarized as follows:

(a) Firstly, the Court must determine if the taxpayer has a source of income from a business for the purpose of section 9 of the *Act*. The ultimate objective of this part of the test is to distinguish between commercial and personal activities (paragraph 50), in accordance with the methodology prescribed by the Supreme Court, especially at paragraphs 52-56, and 60.

(b) Secondly, having found a source of income, a Court must determine if the expenses claimed by the taxpayer may be deducted pursuant to subsection 18(1) from the income earned from the business. If they can, the expenses will be allowed, but only to the extent that they are "reasonable" as required under section 67 (see paragraph 57 of *Stewart*). The Supreme Court emphasized (at paragraph 60):

> Whether or not a business exists is a separate question from the deductibility of expenses.

[31] If we apply the test as outlined in *Stewart* to the facts identified above, the following points should be recognized:

1. The Reasonable Expectation of Profit Test ("REOP") has been rejected by the Supreme Court as a test to determine whether a particular activity is a source of income.

2. Lower Courts are invited to employ the two-stage approach as outlined in paragraph 50 of *Stewart*. In instances where the activities of the parties are not "clearly commercial", as stated in paragraph 53 of *Stewart*, lower Courts are required to consider whether "the activity" has been carried out in accordance with <u>objective standards of business-like behaviour</u> (see paragraph 54 of *Stewart*). Lower

Courts should decide whether "the taxpayer is carrying on the activity in a commercial manner" (paragraph 55 of *Stewart*).

[32] Based on the statements made in *Stewart* and the fact that the nature of the Appellant's endeavours were not "clearly commercial", I must consider whether the "activity" under review meets the tests as outlined above.

Objective standards of business-like behaviour:

I have carefully analyzed all of the evidence and the following points should be noted:

(a) None of the four Appellants made any profit from the purchase of a licence to market the Quest Prestige Cards in a specified territory or from the purchase of a share in territories in Texas through Stellar Dynamic Limited Partnership. (Note: Only the Appellant and Mr. Storwick were involved in the Partnership.)

(b) Furthermore, it appears that there was no chance that any of the Appellants would ever realize a profit from the sale of Quest Prestige Cards because they were each required to provide Rockhaven with the entire $5 per card that was received from Crusader, upon a sale.

(c) None of the Appellants provided any evidence of experience in marketing a product in a definable territory.

(d) None of the Appellants gave evidence of any intended course of action to produce a profit from selling Quest Prestige Cards in the specified territories.

(e) Based on the evidence provided, I have concluded that the sale of the Quest Prestige Card was incapable of ever producing a profit because Crusader did not appear to have a source of funding to carry on a sales campaign. Crusader also had no confirmed source of compensation for their services and appeared to be controlled by related persons.

(f) In his argument, Counsel for the Respondent said that the Quest Prestige Card promotion was not a business opportunity offered to the Appellant, rather it was a tax refund scam perpetrated on these individuals (underlining added).

[33] Counsel for the Respondent said at page 28 of his written submissions:

> *… This is not a case of a business that suffered losses because it was ill conceived or poorly managed, and the tax authorities are second guessing the business acumen of a taxpayer. This is a case where, in fact, there was no business. There were no business expenses. There is no factual foundation for any of the deductions claimed by the appellants …*
>
> **Overview**: It appears that the Appellants were duped into thinking that Crusader would market the Quest Card for them. The Appellants' belief that they had invested in a business opportunity does not make the Quest Card promotion a commercial activity. Through their evidence, and the absence of any evidence from the promoters, it is apparent that the Appellants were victims of a scam. Regardless, a deduction cannot be allowed to the Appellants in the absence of the pursuit of profit in a legitimate business activity. "Put simply, other Canadian taxpayers should not have to bear the financial burden which arises from unfortunate circumstances".

[34] In my opinion, the activity engaged in by the four Appellants of selling the Quest Prestige Card and the activity of the Partnership do not meet the test of objective standards of business-like behaviour as referred to in *Stewart* for the reasons outlined above.

[35] In further support of his argument, Counsel for the Respondent referred to various Court decisions which involved taxpayers who had invested in numerous promotions made by Henry N. Thill.

[36] Counsel for the Respondent said that the structure used by Mr. Allen and the other promoters of the Quest Prestige Card was virtually identical to the structure that was used by Henry N. Thill in numerous promotions.

[37] One of the main "Henry N. Thill" type cases cited by Counsel for the Respondent was *Maloney v. The Queen*, 1989 CTC 213. In that case, Mr. Justice Joyal of the Federal Court held that the true intent of Mr. Maloney and the other Appellants was not to pursue a profitable business opportunity, but rather to avail themselves of the attractive tax deduction the scheme would provide to them.

[38] Mr. Maloney appealed the decision of the Federal Court to the Federal Court of Appeal (see *Maloney v. The Queen*, 92 DTC 6570).

[39] In dismissing the appeal, Justice Hugessen said:

> While it is trite law that a taxpayer may so arrange his business as to attract the least possible tax (see *Duke of Westminster's* case, [1936] A.C. 1), **it is equally clear in our view that the reduction of his own tax cannot by itself be a taxpayer's business for the purpose of the *Income Tax Act*** … To put the matter another way, for an activity to qualify as a "business" the expenses of which are deductible under paragraph 18(1)(a) it must not only be one engaged in by the taxpayer with a reasonable expectation of profit, but that **profit must be anticipated to flow from the activity itself rather than exclusively from the provisions of the taxing statute**.
>
> (Emphasis added)

[40] Various decisions of the Tax Court followed the decision of *Maloney*. I refer to the following cases involving "Henry N. Thill" promotions:

(a) *Bendall v. The Queen,* 96 DTC 1626;
(b) *La Liberté v. The Queen*, 96 DTC 1483;
(c) *Schatroph v. Canada*, [1997] 3 C.T.C. 2148;
(d) *Burton v. The Queen*, 98 DTC 2064;
(e) *Lorenz v. Canada*, [1997] 1 C.T.C. 2484; and
(f) *McPherson v. Canada*, 2006 TCC 648.

[41] In *Burton*, Justice Beaubier said that the operation was not organized to carry on business for profit. Justice Beaubier said "it was a tax loss scheme, pure and simple".

[42] I have reviewed all of the above Court decisions plus a number of other decisions involving Henry N. Thill tax schemes. In my opinion the decisions involving Mr. Thill remain "good law" in spite of the fact that the *Stewart* decision has rejected the REOP test.

[43] In my opinion the activity of the Appellant to become a Quest Prestige Card distributor, either personally or through the Partnership, was not a source of income for the purpose of section 9 of the *Act*.

II. Tax Shelter Rules

[44] Section 143.2 of the *Act* provides for an adjustment to the cost of expenditures relating to a tax shelter investment.

[45] A "tax shelter investment" is defined in subsection 143.2(1) of the *Act*. A "tax shelter investment", means a property that is a tax shelter for the purpose of subsection 237.1(1) of the *Act*, which requires mandatory registration and reporting requirements for "tax shelters".

[46] The Partnership filed and received a tax shelter identification number as required under section 237.1 of the *Act* with respect to the "research and development and customer loyalty card" [Exhibit 2, Tab 2, Form T5001E]. It therefore follows that section 143.2 of the *Act* applies in the present appeal.

[47] Notwithstanding any other provision of the *Act* subsection 143.2(6) calculates the expenditure amount in respect of a tax shelter investment, which is essentially the amount of a taxpayer's expenditure before applying the rules, reduced by deducting the total of:

> (i) limited recourse amounts that can reasonably be considered to be related to the expenditure;
>
> (ii) at-risk adjustment in respect of the expenditure; and
>
> (iii) limited recourse amount and at-risk adjustment of each taxpayer who deals at arm's length with the taxpayer and holds an interest in the taxpayer, that can reasonably be considered related to the expenditure.

[48] The expenditure with respect to the tax shelter investment was the $20,000 royalty amount, which was reported on the Summary Tax Shelter Information Form [Form 5003E].

[49] In the *Tolhoek v. Canada* decision, 2006 TCC 681 confirmed (2008 FCA 128), Madam Justice Campbell states that the unpaid principle of certain long term debt will be deemed to be a limited-recourse amount unless all of the exception in subsection 143.2(7) of the *Act* applies.[2]

[50] The first five exceptions to be met are found in paragraph 143.2(7)(a) of the *Act*, summarized as follows:

> 1. *bona fide* arrangements
> 2. evidenced in writing;
> 3. made at the time the indebtedness arose;

[2] *Tolhoek v. R* 2006 TCC 681 at paragraph 14.

4. made for the purposes of repayment of debt and all interest; and
5. that the arrangements were made within a reasonable period, no longer than 10 years.

[51] The remaining two exceptions can be found in paragraph 143.2(7)(b) of the *Act*, referred to by Madam Justice Campbell at paragraph 41:

1. interest must be payable at least annually at the prescribed rate; and

2. the interest must be paid no later than 60 days after the end of each taxation year of the debtor that ends in the period.

[52] In the present appeal the $15,000 unpaid balance of the Advanced Royalty due under each Licence Agreement was not made with *bona fide* arrangements for repayment and no interest was levied on these outstanding balances. As such the full $15,000 would be regarded as the limited-recourse amount and deducted from the expenditure of $20,000.

[53] Subsection 143.2(2) of the *Act* sets out what is meant by the term "at-risk adjustment", the provision reads as follows:

> **(2) At-risk adjustment** -- For the purpose of this section, an at-risk adjustment in respect of an expenditure of a particular taxpayer, other than the cost of a partnership interest to which subsection 96(2.2) applies, means **any amount or benefit that the particular taxpayer, or another taxpayer not dealing at arm's length with the particular taxpayer, is entitled, either immediately or in the future and either absolutely or contingently,** to receive or to obtain, whether by way of reimbursement, compensation, revenue guarantee, proceeds of disposition, loan or any other form of indebtedness, or in any other form or manner whatever, **granted or to be granted for the purpose of reducing the impact, in whole or in part, of any loss that the particular taxpayer may sustain in respect of the expenditure** or, where the expenditure is the cost or capital cost of a property, any loss from the holding or disposition of the property.
>
> (Emphasis added)

[54] The at-risk adjustment would be the $15,000 performance bond that Crusader had promised to establish since this amount was contingently entitled to the Appellant and the Partnership, for the purpose of reducing the impact, in whole or in part, of any loss that may have been sustained in respect of the investment.

[55] Due to the application of the tax shelter rules, the Advanced Royalties expense would be reduced to zero and as such no deduction would be permitted.

[56] By virtue of the application of the tax shelter rules, there is no longer an expense relating to the investment in the Quest Prestige Card, the arguments and provisions outlined in subparagraphs 23(c), (d) and (e) above would no longer apply.

III. Licence Fee

> When an expenditure is made, not only once and for all, but with a view to bringing into existence an asset or an advantage for the enduring benefit of a trade, I think that there is very good reason (in the absence of special circumstances leading to an opposite conclusion) for treating such an expenditure as properly attributable not to revenue but to capital [*British Insulated & Helsby Cables Ltd. v. Atherton*, 10 T.C. 155, at 192].

[57] The Licence Agreement entered into with Rockhaven required the Appellant and the Partnership to pay a $350 licence fee. Due to the enduring benefit that resulted from this one time payment (i.e. a 20-year licence to sell the Quest Prestige Card in assigned territories) the full $350 would be regarded as a capital outlay and both the Appellant and the Partnership would be precluded from a current deduction due to the application of paragraph 18(1)(b) of the *Act*.

[58] Pursuant to Schedule II of the *Income Tax Regulations* the licence acquired from Rockhaven would fall in Class 14 for the purposes of the capital cost allowance rules, such classification would result in the $350 payment being capitalized and amortized over the life of the Licence Agreement (i.e. 20 years).

IV. Partnership Losses

[59] The evidence presented at trial indicated that the Partnership was not a party to the joint venture. Not only was the agreement between Manhattan and IDC, but the initial investment amount of $320,000, which was subsequently expensed resulting in the allocated losses, was paid by Manhattan. There were no written or oral submissions presented by the Appellant to refute these facts.

[60] After analyzing the facts in the Appellant's case, I have concluded that neither the Appellant nor the Partnership were eligible to deduct the allocated partnership losses.

[61] Based upon the reasons outlined above, the appeals are dismissed, with costs.

Signed at Toronto, Ontario, this 2nd day of May 2008.

"L.M. Little"

Little J.

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APPEARANCES:

Counsel for the Appellant:	James G. Shea and Matt Clark
Counsel for the Respondent:	John O'Callaghan and Chang Du

COUNSEL OF RECORD:

Counsel for the Appellant:

Name:	James G. Shea and Matt Clark
Firm:	Shea Nerland Calnan Calgary, Alberta
For the Respondent:	John H. Sims, Q.C. Deputy Attorney General of Canada Ottawa, Canada