October 31, 2011

BRIEFING NOTE TO MEMBERS OF THE HOUSE OF COMMONS STANDING COMMITTEE ON FINANCE ON TAX INCENTIVES FOR CHARITABLE DONATIONS

This briefing note is submitted in support of the social and economic benefits of reinstating the pre-March 22, 2011 tax treatment of the subscription and donation of Flow-Through Shares. It demonstrates the impacts and loss of benefits for Canada – especially in Ontario since the budget date.

All facts and assumptions set out herein are directly verifiable by the Government of Canada.

Fact – Prior to the March budget, the adoption of the flow-through donation format was growing at approximately forty percent per year and represented a very valuable market force in support of charity and mining without tax cost to the country. Unfortunately, the projected losses associated with implementation of the March 22 budget proposals have now been demonstrated.

Since March, Ontario alone has lost over $ 100 million in direct rural mining industry jobs that would have been funded through flow through financings by donor subscribers. This equates to over $ 65 million in donations since March. The budget changes represent a negative economic and social price for Canada.

Introduction: The March 2011 Federal Budget introduced a measure ("**Budget Proposal 34**") that would have the impact of virtually eliminating a powerful philanthropic tool – flow through donation financing gifting arrangements ("**FTDF**"). Following the 2006 introduction by the Harper Government of an exemption from capital gains tax arising on the donation of publicly listed shares (including flow through shares), the founder of Peartree Financial Services Ltd. laid the groundwork for an innovative financing structure that would enable millions of dollars of charitable donations. Largely comprised of entrepreneurial owner/managers and professionals, flow through donation gifting arrangements provided Peartree clients with an opportunity to benefit their communities that they would not otherwise have.

Background: FTDF combines two well established tax incentives in a manner that has the effect of both generating new investment for junior resource companies and increasing and accelerating charitable giving. Prior to the March 2011 Federal Budget, this was accomplished through the following steps:

1. A subscriber/donor purchases flow through shares issued by a Canadian junior mining company providing a tax deduction for the donor in the amount of the purchase price for those shares spent on Canadian mineral exploration expenses (and associated credits);
2. The shares are donated to charity by the subscriber (Although the cost base of the shares is deemed to be reduced by the amount of the flow through deductions available to the donor, the disposition of the shares by way of donation does not attract capital gains tax);

3. The recipient charity issues a charitable receipt to the donor in the amount of the proceeds of sale realized by the charity.

In 2010, FTDF delivered over $125 million of donations to registered Canadian charities and raised over $200 million in mineral exploration risk capital for junior mining companies spent largely on jobs in remote northern and Aboriginal communities.

Impact: Without FTDF, our clients have told us that major charitable gifts are at risk - gifts that provide much needed programming and services for Canada's most vulnerable communities. Numerous charities have expressed their concerns to us. For example, The Ottawa Regional Cancer Foundation has written to say:

"Our experience is that with flow-through shares, donors have been giving three to five times more.... If donors cannot honour commitments because of the removal of this giving option, or if they extend their payment schedule, it will put programs at risk and mean we will hire fewer cancer coaches, deliver fewer programs and provide fewer services than had been planned, for patients and families. And quantitative research has demonstrated that these services improve patients' quality of life, extend life expectancy, and decrease the cost to the health-care system."

Extracts from other letters written to the Minister of Finance attesting to the positive impact of FTDF to both charities and resource exploration companies are attached hereto as **Appendix A**. Full copies of these letters and our other briefing materials are available on request.

Alignment with Government Priorities: While acknowledging the benefits provided by FTDF, the Ministry of Finance took the position that its review of FTDF had to be confined to an analysis of the tax support available to a donor of flow through shares without any consideration of the economic and social benefits provided to the resource sector and charitable organizations. The Harper government's own most recent statement of priorities emphasizes (1) job creation, (2) development of economic opportunities for northern communities, and (3) support for families. FTDF fosters all of these important national objectives by

- providing much needed financing for Canadian resource exploration which is a mainstay of Canada's economy
- increasing and accelerating major charitable donations including donations to public institutions such as hospitals, universities and cultural facilities offsetting some of the demand on the government to support services offered by these institutions
- contributing to economic development in remote northern and First Nations communities in which families are often dependant on the ability to secure work with companies conducting resource exploration

Tax Integrity: The document attached hereto as **Appendix B** illustrates how FTDF actually maintains the integrity of the tax base, but moves resources through the economy in a way that generates economic activity, simply rearranging the government's source of tax revenue.

The deductions available to a charitable donor in respect of an investment in junior mining company exploration is an inclusion in the income of families earning their livelihood in communities such as Val d'Or and Timmins. The funds going to the recipient charities will ultimately be used for programs requiring services and equipment that also generate jobs and taxable income.

In its 2010 report, "*Mobilizing Private Capital for Public Good*", the Canadian Task Force on Social Finance stated "Evidence indicates that the modest costs of [tax incentives to encourage private investors to close the funding gap of] social enterprises are more than offset by the double returns that ensue ie. meeting a broad range of community needs and creating new jobs and economic growth."

After the Budget: The prognostications of interested parties shortly following the introduction of the March 2011 Budget may have seemed speculative at the time. However, now that we have had six months to experience the effects of the measure to eliminate the capital gains exemption on the donation of flow through shares, there is actual evidence to support our position that this measure has negatively impacted both philanthropy and mineral exploration in this country.

Due to the fragile state of the global economy and stock market volatility, high risk exploration financing is very difficult to secure. It is especially in these challenging times that the transaction structure of FTDF can provide a financing alternative that is not otherwise available. In 2009 when markets turned down significantly, FTDF arranged by PearTree enabled a number of flow through financings that otherwise would have been aborted. While some FTDF transactions are being done in the Province of Quebec due to the provincial incentives offered by the Quebec government (including a capital gains tax exemption on any disposition of flow through shares), there has been almost no activity across the rest of the country since March.

We deal regularly with numerous charitable organizations across the country. It has been expressed to us that major charitable gifts are down as a direct result of the increased after tax cost of donations via FTDF since the Budget. This is supported by academic research that has studied the impact of the changes in the tax treatment of donations of securities (see the Memorandum from A. Abigail Payne, Ph.D. Economics, Professor attached as **Appendix C**).

Overstated Tax Savings: Furthermore, even if Budget Proposal 34 is considered solely with reference to projected taxes that will become collectible from flow through share donors, the tax savings projected in the budget materials were significantly overestimated. Donors generally buy flow through shares solely for the purposes of donating them to charity, and rarely for investment. As a result of Budget Proposal 34, most donors will simply not buy flow through shares for donation purposes. Consequently, there will be fewer donations of flow through shares, fewer capital gains and less tax payable. In the words of a typical Peartree client:

"Previous to this structure we never purchased flow through shares for investment or tax purposes. In the absence of this program, we will not again. It is unlikely that there will be any recovered capital gains tax on my flow through share investment this year since the investment will not be made in the first place."

Six months following the budget, this can be shown to be true. Our briefing book delivered to the Ministry of Finance in May of this year provides clear direction as to how the government can substantiate our claims with information available to the government, but not to us.

No abuse: Our services have been subject to the highest level of scrutiny both through the process of obtaining advance tax rulings from CRA and Revenu Quebec and through rigorous due diligence exercises by clients. We are extremely troubled by unscrupulous behaviour by those who have alleged to be acting in the best interests of charity. We have numerous clients who would not be willing to risk their reputations on involvement with an arrangement without being completely satisfied with its propriety. In this regard, we refer you to letters supporting FTDF submitted to the Finance Minister by Rudolph Bratty and Purdy Crawford.

Recommendation: For the reasons articulated above, we submit that Budget Proposal 34 be modified to allow FTDF to continue to provide the support desperately needed by Canada's charitable sector. Specifically, we respectfully propose an amendment to section 4 of Bill C-13 that would have the effect of reducing rather than eliminating the capital gains tax exemption available on the donation of flow through shares ie. tax 25% of the capital gain rather than 50%. In line with this and to preserve tax integration as between income earned directly or through corporations, we recommend that the pre-budget treatment of the CDA account be restored to the same extent that an exemption is maintained in respect of capital gains tax payable on the donation of flow through shares.

We respectfully request your support in bringing this matter forward to the Finance Committee as a whole with the objective of the Committee making our proposal a priority in its recommendations regarding charitable giving to Parliament.

Proposed Solution addresses Government concern: In suggesting our recommended amendment to section 4 of Bill C-13, we recognize and accept that the Government may be uncomfortable with the level of tax support for a charitable gift through a flow through donation arrangement. We believe the compromise position being put forward allows the Government to be a proud champion of a multitude of causes vital to our Canadian society without being criticized for being overly generous to a specific group of taxpayers. We remind the Committee members that our requested amendment to Bill C-13 would reinstate the regime for the donation of flow through shares that was in place prior to 2006.

Conclusion: The Committee has been charged with a review of this matter with a view to encouraging increased charitable giving. We are mindful of the current fiscal situation of the federal government. However, we respectfully submit that an analysis of the impact of the availability of a capital gains exemption for the donation of flow through shares must take into account the benefits to Canadian charities and resource companies and the constituencies they support and serve. It must also consider the change in behaviour of philanthropists who will no longer be induced to purchase flow through shares which will demonstrate that the magnitude of the predicted tax savings from the introduction of Budget Proposal 34 has been overstated.