

BACKGROUND

Changing the rules is harming individual, hard-working Canadians and their families

Trusts are owned by ordinary people who have invested in the Canadian economy and were dealt a \$35 billion blow to their net worth in two days.

- Retroactively changing rules has negatively impacted individual Unitholders and other Canadians directly and through their investments in mutual funds and group pension funds including the Canada Pension Plan.
- The change has also negatively affected

Investors in Canadian corporations through erosion of investor confidence domestically and globally

Employees and contractors of Trusts

All Canadians who saw capital gains turn into losses

Charitable organizations

Follow on recipients of re-investment of distributions, either through capital investments or within the economy.

- Trusts are owned largely by retail investors. Individuals have been investing hard-earned capital and planning for their own savings and retirement. Millions of Unitholders who have followed the rules and acted in good faith in making their investment decisions have now been penalized with 20% investment losses.
- Investors have come to rely on income from Trusts to support their current standard of living. The Income Trust sector provides a reliable investment vehicle for investors with a need for income, including retirees and those on fixed incomes.
- For many Canadians this steady stream of income is a necessity, not a luxury.
- In the present low-interest rate environment, Trust capital is drawn from GICs and other passive investments, not from other equity investments.
- The group of investors will grow as the large baby boomer generation enters their retirement years. Over 70% of Canadian workers do not have defined benefit pension plans and are reliant upon their RRSP investments.
- With an aging population in Canada, there is an increasing demand for income generating investments. Financial planning options have suddenly become more limited. This has happened in the face of the Canada Pension Plan becoming increasingly inadequate to meet the needs of the growing number of retirees relative to the number of people in the workforce.

- Income Trusts provided an alternative investment and risk/return profile relative to corporations that are targeting high growth and capital appreciation.
- The Trust structure provides a high level of transparency and accountability to the investor as cash flows are closely monitored.
- Based upon the current distributions paid monthly by all Energy Trusts in Canada, over \$7 billion will be paid to Unitholders in 2006, who in turn reinvest in local economies, promoting reinvestment and creating jobs.

Energy Trusts are Essential to Canada's Economy and to Canada's Role as a Global Energy Provider

Energy Trusts play a unique and integral role in maximizing oil and gas production and providing essential capital to Canada's strategically important energy industry.

- An important symbiotic relationship exists between Senior integrated oil and gas corporations, Trusts and Junior exploration and production companies.

Energy Trusts provide capital to the senior E&P companies by buying the maturing assets which they perceive to be of limited value.

Energy Trusts create an exit strategy for junior oil and gas companies, as the logical buyers of their assets once they have proven up new reserves.

Over \$20 billion of new capital has been injected into the energy sector through energy Trusts in the last five years. Much of this capital has been deployed to find new oil and gas by senior corporations that have sold assets for cash to reinvest, by junior oil and gas company management that have sold companies for cash to reinvest again and by Trusts themselves.

Energy Trusts have themselves made over \$10 billion of capital investment into the finding and development of oil and gas in Canada.

- The Western Canada Sedimentary Basin is mature; light oil supplies are declining; natural gas supplies are declining. Energy Royalty Trusts were established to maximize production of this depleting resource. Capital-efficient Trusts work to extract “every last drop” from mature oil and gas reservoirs in Canada and invest in assets that major oil firms have deemed too small and time-consuming to develop. Trusts account for almost 20 percent of Canadian crude oil and natural gas output.
- Without the energy Trusts, the investment in such fields and overall Canadian production will continue to decline further (along with royalties paid to provincial governments). There would also be a significant drop in royalty and other revenue to a number of provinces – including Newfoundland, Nova Scotia, Ontario, Saskatchewan, Manitoba, BC and Alberta – all of which would increase the financial pressures on the federal government.
- Canada has long been a resource rich and capital poor (in a relative sense) nation that needs and encourages foreign investment. The loss of energy Trusts will reduce the total amount of investment capital available in a capital intensive industry. Many investors – including many foreign investors – would never buy an E&P company but have invested in Trusts because of their lower risk profile and income-yielding nature.

- Approximately \$9 billion of foreign-controlled assets have been acquired by Canadian energy Trusts since 2001, reversing a trend of increasing foreign ownership in the Canadian energy sector. Without the energy Trusts, Canada's energy sector will be challenged to compete against international companies from lower tax regimes. The proposed rules could leave energy Trusts vulnerable to foreign takeovers, resulting in less Canadian control of this strategically important sector.
- Energy Trusts invest heavily in new technologies and engineering processes to successfully maximize production. Research and development examples are prevalent throughout the Trust sector. These include such projects as CO₂ injection into coal for enhanced coal bed methane recovery, CO₂ enhanced oil recovery projects, proposed SAGD projects for subsurface bitumen recovery and improved oil sands recovery technologies.

A Tax Policy of Such Significance Warrants Serious Consultation and We Want to be Consulted.

We are asking for that consultation because we have an important perspective to contribute.

- We should be proud of the innovation inherent in Canada's Trust sector.
- A one-dimensional solution has been proposed to what was perceived as a problem: the conversion of large tax-paying corporations. Stopping the conversions is one thing; eliminating the Trust structure is another.
- Retroactively changing rules is not good public policy and will damage Canada's international reputation, affecting our ability to raise capital abroad.
- Energy Trusts made capital investments in good faith based upon what was allowed under Canadian law.
- The government excluded REITs from its recent decision, recognizing the important role they play in the economy. Like REITs, energy Trusts have a 20-year history of value creation in Canada and they compete internationally for capital.
- Like REITs, the energy Trust model has proved to be useful for managing assets efficiently rather than solely for tax purposes.

- The change results in an un-level playing field – the master limited partnership structure in the US is the American equivalent of the Canadian energy Trust. It too is recognized as an efficient structure for harvesting mature energy resources.
- The government has expressed concern about tax leakage – under the new policy they announced, there could be even more tax leakage if these Trusts are sold to foreign entities or converted to private entities, and debt financed - in which case, neither they nor the Unitholders pay taxes.
- Canadian productivity would improve if the government instead chose to tax corporations to be competitive with Trusts instead of taxing trusts to be competitive with corporations.
- With new conversions effectively stopped for now, this is the time to consult with industry. There is no need to rush the passage of new legislation.
- A phase out period that results in a 15 to 20 percent (\$35 billion) catastrophic reduction in market capitalization is clearly not the answer.