

CAIF

CANADIAN ASSOCIATION
OF INCOME FUNDS

L'ASSOCIATION CANADIENNE
DES FONDS DE REVENU

ACFR

Canadian Association of Income Funds

Presentation on Foreign Ownership Restrictions
September 2004

Agenda

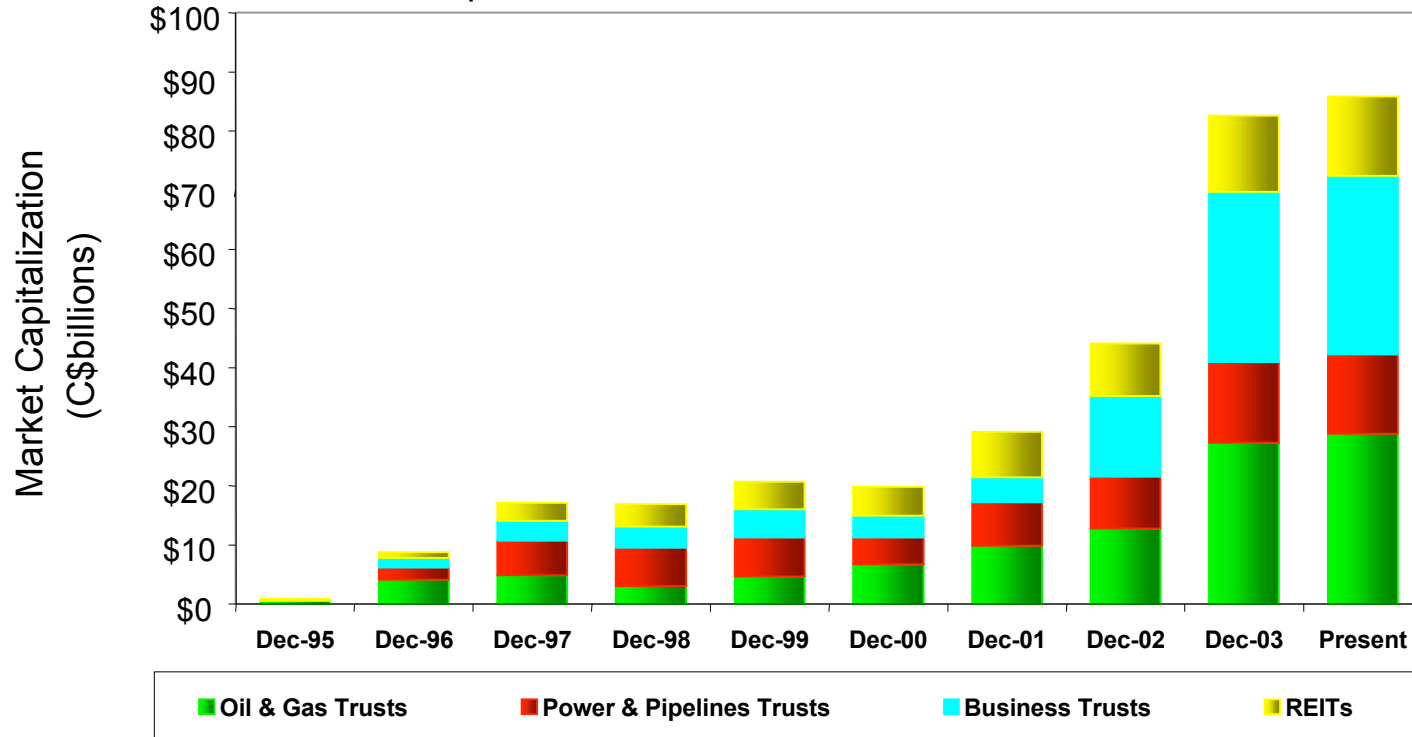


- Background information on Trusts in Canada
- What is CAIF?
- The proposed changes to the Tax Act affecting Trusts in the 2004 federal Budget
- The need for foreign capital in Canada
- The benefits of Trusts in Canada
- Consequences of restricting foreign ownership
- The question of tax leakage
- What are we asking?

Canadian Income Trust Growth



- The Trust sector has grown by over 400% in the last 5 years
- With a market capitalization of almost \$90 billion, Trusts comprise almost 10% of the TSX
- Oil & Gas Trusts represent 34% of the total Trust market



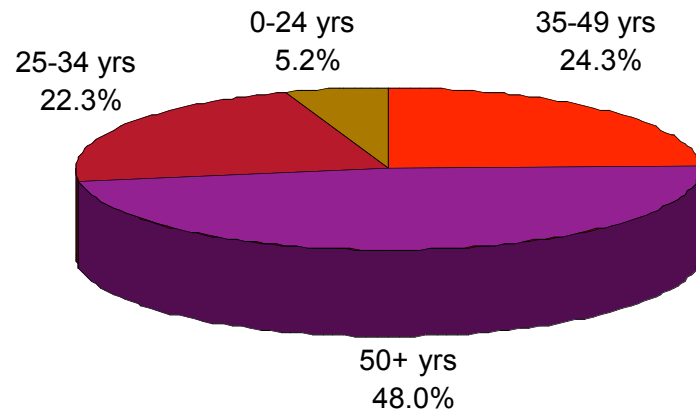
Source: RBC Capital Markets

Who Owns Trusts in Canada



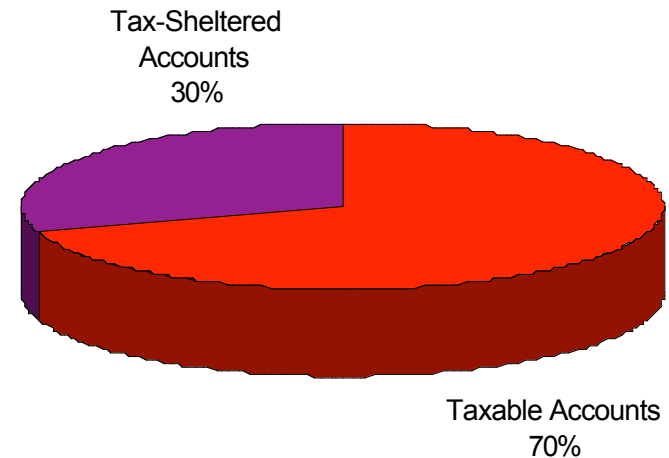
- Retail investors represent approximately 80% of income trust holders

ESTIMATED AGE OF UNITHOLDERS



Source: Estimations based upon results of Canada Newswire survey of investors seeking information on PrimeWest Energy Trust and Enerplus Resources Fund

ACCOUNT TYPE

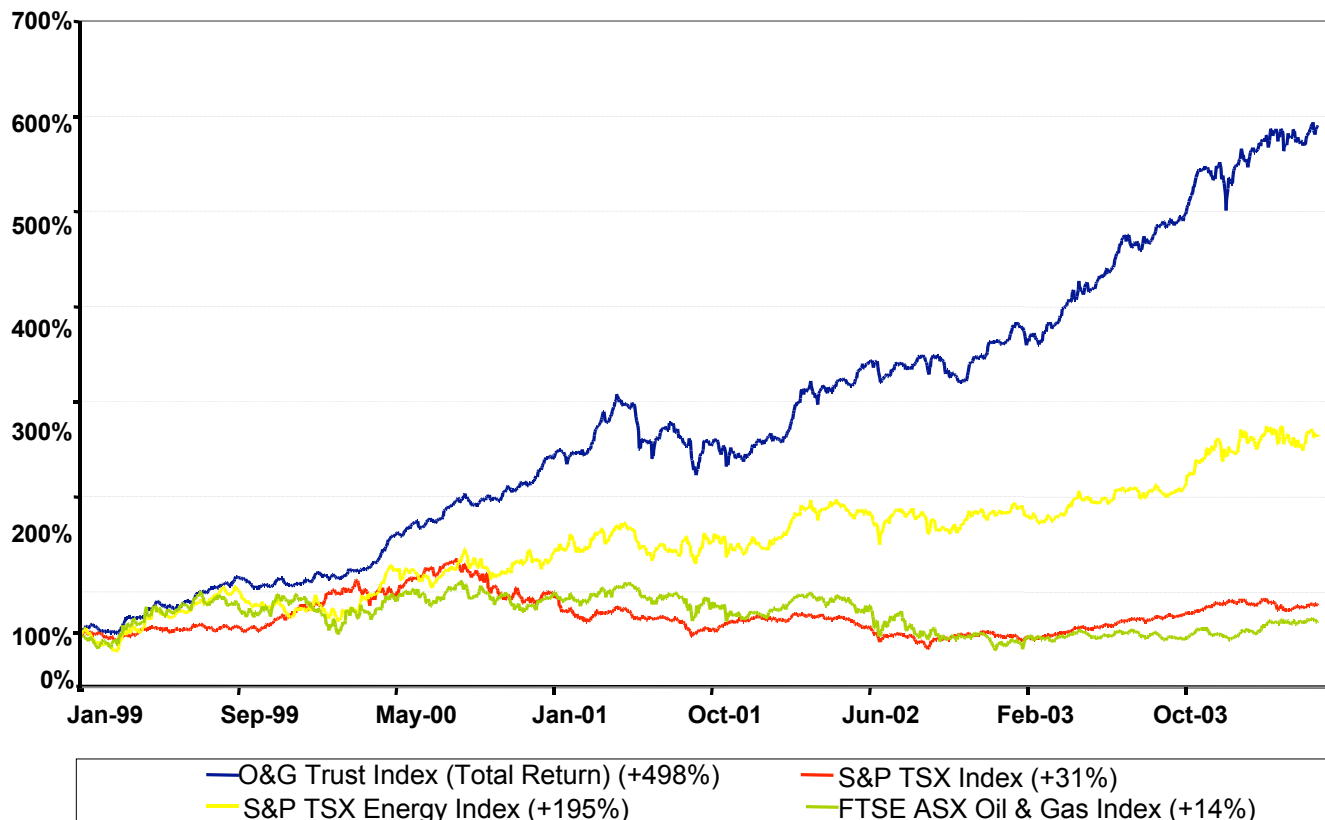


Source: BMO Nesbitt Burns, CIBC World Markets and RBC Capital Markets

Trust Performance



- Since 1999, the Oil and Gas Trust Index has outperformed the TSX Composite Index by 16.1x and the TSX Energy Index by 2.6x



Source: RBC Capital Markets

CAIF



- The Canadian Association of Income Funds (“CAIF”) represents over 25 Trusts from various sectors with a combined market capitalization of \$30 billion
- The CEOs in attendance represent five of the largest oil and natural gas Trusts in Canada with an aggregate market capitalization of approximately \$15 billion
- These Trusts produce, in aggregate, over 300,000 BOE per day of oil and natural gas and directly employ approximately 2,000 personnel throughout western Canada

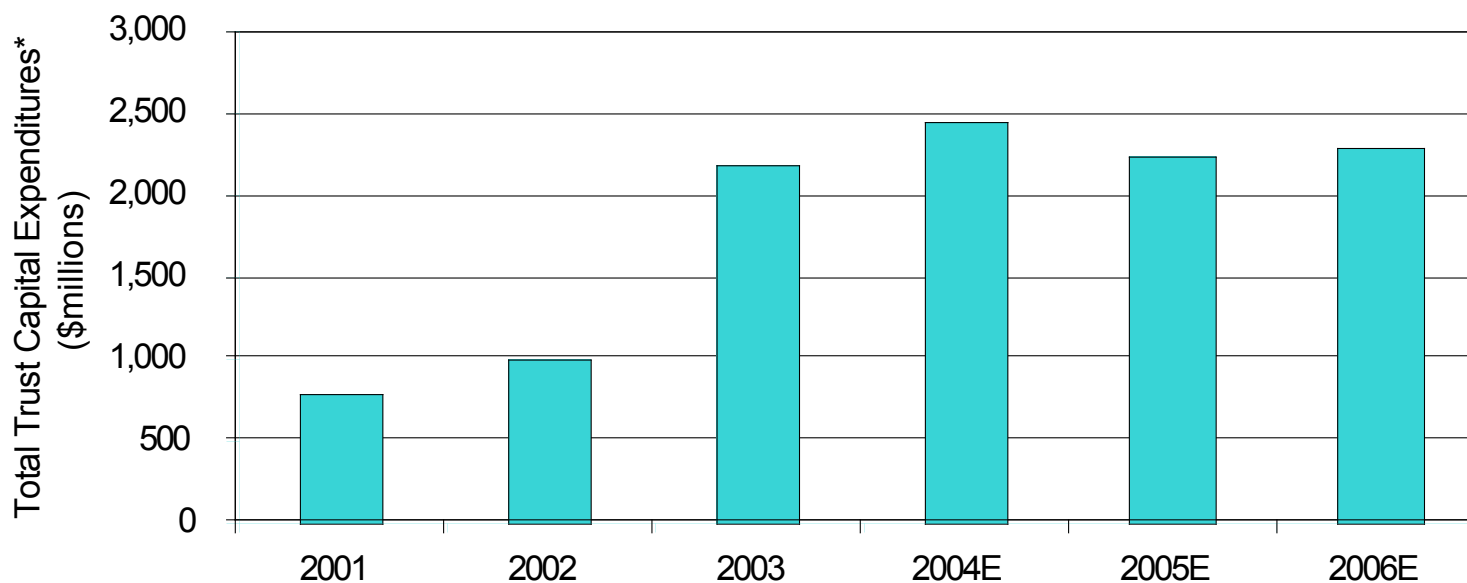
Proposed Changes in 2004 Federal Budget



- The Federal government is proposing to make certain changes to the Canadian Income Tax Act that would have adverse affects on the economic viability of Trusts in Canada:
 - The definition of Taxable Canadian Property would be changed so that resource and timber based Trusts would be subject to foreign ownership restrictions
 - All Trust distributions paid to non-residents would be subject to a 15% withholding tax, including otherwise non-taxable types of distributions that are currently exempt
 - Restrictions on ownership in certain types of trusts by Pension Funds (currently suspended pending further discussion)

The Need for Foreign Capital in Canada

- Increasing amounts of capital are needed to develop Canada's oil and natural gas reserves and large scale projects such as Oil Sands, SAGD, primary, secondary and tertiary recovery schemes
- Canadian Trusts, by virtue of their distribution model, pay out more cash flow to investors and have an increasing need for access to capital for re-investment



* Excludes acquisitions

Source: FirstEnergy

The Need for Foreign Capital in Canada

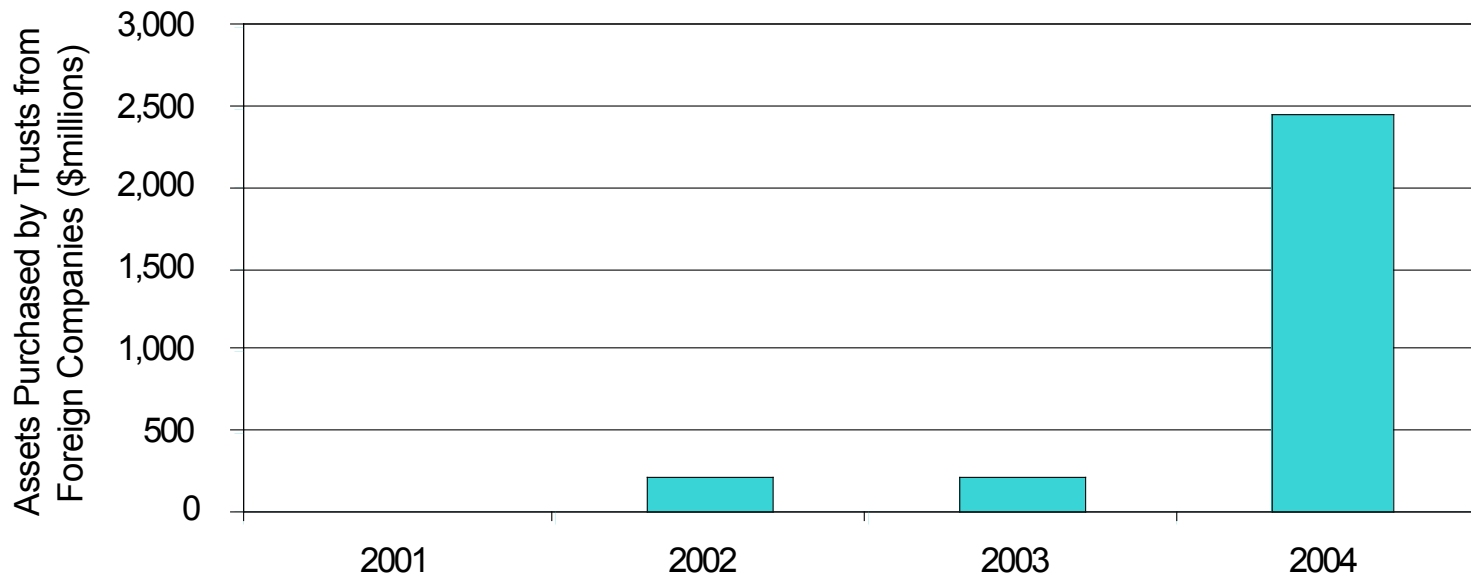


- Energy is one of Canada's most important resources. Maximizing the extraction of our oil and natural gas resources benefits all Canadians
- The Canadian capital markets may not be able to absorb the significant amount of capital needed to fully exploit our reserves over the long term
- Trusts must therefore find additional capital sources outside of Canada
- The Canadian resource sector has a long history of foreign investment
- Foreign investments into Canadian resources ultimately creates employment and revenues, both at the Provincial and Federal levels

The Benefits of Trusts



- Oil and gas Trusts purchase many Canadian assets from foreign companies thus transferring the mind and management of these assets back into Canada
- In 2004 alone, Canadian Trusts have purchased assets from U.S. companies such as Chevron/Texaco, Murphy Oil, Calpine Corp., Williams, Anadarko Petroleum Corp. and El Paso Energy



Source:
FirstEnergy

The Benefits of Trusts



- Trusts have been able to re-enter mature areas of the Western Canadian Sedimentary Basin that have had little or no recent development activity stimulating incremental production and reserves growth and fueling local economies
- The increased drilling activity brought about by Trusts has created numerous jobs and helped boost Canada's oil and gas exports to record levels
- Trusts are now starting to purchase assets outside of Canada and are importing cash flows from other countries into Canada
- Trusts are increasing the amount of investment in secondary and tertiary recovery schemes of mature Canadian oil and natural gas fields

Consequences of Foreign Restrictions



- Due to market size and product saturation, the Canadian capital markets can only support equity offerings of limited size
- By subjecting resource Trusts to foreign ownership restrictions, the Federal government would severely limited the ability of Trusts to participate in the development of large scale projects
- As foreign and Canadian companies sell larger assets, Trusts would be competitively challenged in situations where significant funds are required to compete for opportunities
- Several Trusts already have a majority of foreign ownership and would have to somehow repatriate hundreds of millions of dollars worth of Units at great cost to their existing Canadian Unitholders. This could result in significant market disruption and unwarranted economic losses in the Canadian retail market

Government Concerns - Tax Leakage



- We suspect the budgetary changes came as a result of government concerns over tax leakage
- CAIF commissioned a study by HLB Decision Economics Inc. to analyze the proposed budgetary tax changes related to non-resident taxation, (attached)
- The key findings of the study were:
 - Increased withholding taxes on the otherwise non-taxable portion of foreign distributions would increase government revenues by \$83 million in 2004
 - Tax losses due to increased foreign ownership, however, are relatively minimal – post budget effects of changes to withholding taxes would more than compensate for that reduction
 - Where non-resident investment shifted from oil and gas corporations to Trusts, a net increase in tax revenue was seen in every case

Government Concerns – Tax Leakage



- The following points illustrate the effects on tax revenue from foreign ownership of Canadian Trusts
 - On average, 61.3% of trust distributions were taxable in 2003 in the hands of Canadian unitholders, while the remainder was tax deferred as a return-of-capital
 - 30% of trust holdings in the Canadian retail market are estimated to be held in non-taxable accounts (RRSP's, RRIF's, RESP's etc.)
 - If we use an individual tax rate of 35%, the current tax revenue from the Canadian resident unitholder base is therefore 15%
- Considering the 15% tax applied to foreign investors is paid monthly and at source, while the 15% Canadian rate is only paid at year end, the net tax losses are truly minimal, if any

What we are asking



- Include Trusts, along with Canadian pension funds, in the consultation process with market participants on the effects of changes in the Tax Act
- Do not restrict Canadian trust access to foreign equity capital markets by restricting ownership
- Do not change the definition of “Taxable Canadian Property” so that resource based trusts can access foreign equity markets