



**Prospectors & Developers Association of Canada**  
**Association canadienne des prospecteurs et entrepreneurs**

Submission by the  
Prospectors and Developers Association of Canada (PDAC)  
to the House Standing Committee on Finance

Pre-Budget Consultations

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135 King Street East  
Toronto, Ontario, Canada M5C 1G6  
Website: [pdac.ca](http://pdac.ca); email: [info@pdac.ca](mailto:info@pdac.ca)  
Telephone 1 416 362 1969; Fax 1 416 362 0101

## Introduction

This submission is presented by the Prospectors and Developers Association of Canada (PDAC), representing Canada's mineral exploration industry. The PDAC is a national organization with 7,000 members representing the range of companies and individuals in mineral exploration and development. Our corporate members include senior producing companies and junior companies (small and medium enterprises [SMEs]). Our individual members include prospectors, geoscientists, geological and environmental consultants, junior exploration and senior mining company representatives. Our members also include people in the financial, legal, and academic communities, students, and those who supply services and equipment to the mineral industry.

As the 'research and development' branch of the mining sector, exploration companies do not have production revenue and, therefore, must rely on investors who are prepared to support high-risk activities. The global financial crisis and the steep drop in commodity prices are having dramatic and negative effects on the exploration sector. Reduced investment in companies will lead to fewer drilling programs and will impact negatively on regional employment and income, particularly in rural, northern and Aboriginal communities.

Working with our members, the PDAC has developed several proposals as solutions to reduce the impact of the current financial crisis on the mineral industry in Canada, to retain our leadership position in global exploration and to ensure that the mineral sector is a major contributor to Canada's economic recovery and continued growth.

## Federal taxation and program spending priorities

### Responding to the impact of the financial crisis on the mineral industry

PDAC recommendations to ensure that mineral exploration companies survive and contribute to Canada's economic recovery:

#### 1. Tax incentives (Mineral Exploration Tax Credit):

Encourage investment in Canadian projects by temporarily increasing the Mineral Exploration Tax Credit (METC) for exploration financed using flow-through shares from the current 15% rate to 30% for the next two years; and, to ensure longer term investment in Canada, and to allow exploration companies to plan for the future, make the current 15% METC a permanent feature of the federal income tax system.

#### 2. Infrastructure (Transportation and Geo-mapping):

- a. Invest in transportation infrastructure (i.e. all weather roads, bridges, road upgrades, as well as improvements to sea ports and airports) in Canada's north and remote regions of the provinces. All weather roads, in particular, greatly improve the economics of exploration projects, increasing access and allowing for extended exploration seasons (i.e. adding months to exploration in those regions that only have access by winter roads).

- b. Create jobs and retain expertise in Canada's world renowned mineral exploration sector by maintaining a long-term commitment to the **Geo-mapping for Energy and Minerals (GEM)** infrastructure program.

### 3. Issuance and compliance costs associated with exploration companies:

Improve an exploration company's ability to retain employees by allowing **issuance and compliance costs** (i.e. costs associated with financing, legal and accounting expenses) to qualify for renunciation as Canadian Exploration Expense (CEE) under flow-through share arrangements.

We believe these recommendations will have an overall positive impact on the economy without a significant cost to government. However, variations on these proposals, improvements to existing programs, or additional measures may be necessary.

## Longer Term: Maintaining a Vibrant Exploration Sector

A vibrant mineral sector in Canada creates jobs, sustains communities, fosters new business opportunities and raises tax revenues that allow government to meet social needs. In the past few years, the federal government has responded positively to our sector's recommendations through changes to tax policies and investments in specific programs. Examples include the extension of the Mineral Exploration Tax Credit (METC) and the expansion of the Geo-mapping for Energy and Minerals program. In addition to the proposals noted above, the PDAC recommends the following policy initiatives as longer term measures that are intended to support a strong investment climate for the mineral industry in Canada.

### Recommendations to support a continuing strong investment climate for the mineral industry in Canada:

**Clarify CEE definition with respect to former Mine Sites:** the federal government, as part of a long-term strategy for mineral exploration, should clarify that the Canadian Exploration Expense definition includes the costs of carrying out exploration at former mine sites that have not operated for at least 5 years. Treating costs associated with these activities as CEE will promote mineral exploration in Canada in areas that might otherwise be overlooked because of uncertainty about the tax treatment of the expenditures incurred. An objective test for this eligibility would eliminate uncertainty in the application of the existing law, and encourage the discovery of new resources that could help maintain existing mining communities and revive ones that have low levels of activity.

**Provide Flow-Through Share Treatment for QETs:** allow specified costs related to the activities of a Qualified Environmental Trust (QET) to be eligible expenses that can be financed using flow-through shares (FTS). The benefit to governments of allowing FTS treatment for expenditures incurred at abandoned sites is that the cost of the program would be offset by the reduction and/or transfer of the government's financial or environmental liabilities at abandoned sites to the private sector. There will also be benefits from increased economic activity and tax revenues associated with increased exploration and reclamation, as well as economic development and investment from potential discoveries, particularly in remote and northern communities.

## Background on Recommendations

### 1. Tax incentives (Mineral Exploration Tax Credit)

Encourage investment in Canadian projects by temporarily increasing the Mineral Exploration Tax Credit (METC) for exploration financed using flow-through shares from the current 15% rate to 30% for the next two years; and, to ensure longer term investment in Canada, and to allow exploration companies to plan for the future, make the current 15% METC a permanent feature of the federal income tax system.

- Without sufficient investor support, exploration companies face a reduction in or cancellation of programs in 2009, with a resulting impact on service companies and neighbouring communities, including those in remote and northern areas of Canada
- The 15% federal METC is the centerpiece in the current system of federal and provincial exploration tax incentive programs designed to assist flow-through share financing. Almost all major mining provinces in Canada provide additional incentives to supplement the federal credit.
- In the January 2009 federal budget, the METC was extended by one year to March 31, 2010. Funds raised with the credit during the first three months of 2010 can support qualifying exploration until the end of 2011. The net cost of this program to the government is an estimated \$55 million over the next two fiscal years.
- Without sufficient investor support, exploration companies face a reduction in or cancellation of programs in 2009, with a resulting impact on service companies and neighbouring communities, including those in remote and northern areas of Canada. Potential investors are concerned that, even with the 15% METC, future market prices of flow-through shares do not justify the investment.

#### Benefits of a Two-Year Increase in the METC Rate from 15% to 30%

- Increasing the credit rate to 30% would allow the exploration industry to maintain a reasonable level of exploration activity during this period of depressed commodity prices. For a high-income investor in Ontario, for example, it would reduce the after-tax cost per dollar of investment by about 9 cents.
- The after-tax cost would be further reduced if the provinces were to reinforce the proposed federal initiative by increasing their credit rates as well.

#### Benefits of making the 15% METC a permanent feature of the income tax system

- Investor uncertainty about the future of the METC impairs the ability of companies to effectively plan multi-year exploration program financing. It limits the ability of partnerships to market the investments in an orderly and timely manner to new investors. Making this program permanent would increase investor certainty and provide a more rational time-frame for planning and executing exploration programs.

## 2. Infrastructure (Transportation and Geo-mapping)

### Transportation

It is recommended that the federal government invest in transportation infrastructure (i.e. all weather roads, bridges, road upgrades, as well as improvements to sea ports and airports) in **Canada's north and remote regions of the provinces**. All weather roads, in particular, greatly improve the economics of exploration projects, increasing access and allowing for extended exploration seasons (i.e. adding months to exploration in those regions that only have access by winter roads).

A "Roads to Resources" cost-sharing program should be developed to initiate projects that improve road access to minerals. Infrastructure projects should be selected based on their ability to improve access to regions of mineral exploration activity.

### Geo-mapping

Create jobs and retain expertise in Canada's world renowned mineral exploration sector by maintaining a long-term commitment to **the Geo-mapping for Energy and Minerals (GEM)** infrastructure program.

#### Benefits

- The PDAC has long advocated for the expansion of the federal government's geoscience and mapping activities. The PDAC was very pleased with the Prime Minister's 2008 announcement of \$100 million to map the North (the GEM Program) and has recommended in-year increases for 2009 and 2010 in order to retain expertise in the sector during the financial crisis. In May 2009, the Natural Resources Minister announced accelerated funding of \$8 million (increasing GEM from \$22 million to \$30 million in 2009).
- Investment in geoscience research directly benefits both governments and the mineral sector by advancing knowledge and encouraging new exploration activity. A high-quality and easily accessible geoscience database (i.e. geological data and maps) is a key competitive advantage internationally, attracting investment dollars and leading to the discovery of mineral deposits and to the development of new mines.

## 3. Issuance and compliance costs associated with exploration companies

Improve an exploration company's ability to retain employees by allowing **issuance and compliance costs** (i.e. costs associated with financing, legal and accounting expenses) to qualify for renunciation as Canadian Exploration Expense (CEE) under flow-through share arrangements.

#### Benefits

- It is proposed that a portion (e.g. 10-15%) of the overhead expenditures incurred by corporations in carrying out their offering be treated as a Canadian Exploration Expense.
- Many overhead costs are associated with issuing requirements established by provincial law or the rules of stock exchanges. They are a relatively fixed charge associated with share

issuance. Allowing a proportion of these costs to be treated as CEE and therefore eligible for flow-through share treatment will free up funds for grassroots exploration.

- Not all overhead costs are associated with share issuance. In principle, the specific costs associated with share issuance could be separated out. However, such an approach raises difficult definitional questions and uncertainty regarding eligibility.
- The 10-15% proposal substitutes a simple administrative rule which, in turn, provides greater certainty to both issuer and purchaser regarding eligible costs. There is a precedent for this under provincial grant systems which support mineral exploration (e.g. Manitoba). These grant programs usually have a 10-15% ceiling on the amount of eligible overhead expenses. Historically, federal grant programs designed to encourage resource exploration have also included allowances for certain overhead costs.

## Background

- The Income Tax Act places various restrictions on amounts that can be renounced as Canadian Exploration Expenses (CEE) and be financed through the METC.
- Overhead expenses - legal, regulatory and financial costs, etc - are excluded from the CEE definition and thus cannot be financed using flow through shares.
- Although overhead expenses are deductible, the typical junior mining company is not in a tax-paying position and thus is unable to use these deductions for many years.
- Overhead expenses are essentially a fixed cost associated with flow-through share issuance. In the current environment of depressed share prices, the fixed overhead charges severely restrict the funds available to junior mining companies for exploration activity.
- Partnerships which raise money by selling units to new investors may also have overhead expenses. These partnerships often purchase flow-through shares on behalf of their unit holders.