



SEARCH

Programs A-Z

[Home](#) | [NEWS](#) | [Canada AM](#) | [Weather](#) | [Sports](#) | [eTalk](#) | [Programs](#) | [TV Listings](#) | [Contests](#) | [Local Station](#)
[Latest News: Sept. 11th plotter to learn his sentence](#)
[NEWS](#) [Programs](#) [CTV News Team](#) [Services](#)
[Top Stories](#) [CANADA](#) [World](#) [Entertainment](#) [Health](#) [Sports](#) [Business](#) [Sci-Tech](#) [Politics](#) [Consumer](#) [Specials](#) [Galleries](#)

Canada



Income trusts the business story of 2006: CP

Updated Fri. Dec. 29 2006 11:39 AM ET

Canadian Press

TORONTO -- After roiling financial markets and riling investors, the federal government's decision to tax income trusts has been named 2006 Business Story of the Year by The Canadian Press and Broadcast News.

With 52 votes from newspaper and online business editors and broadcasters out of 139 cast across the country, the trust furore was by far seen as Canada's most compelling business news item of the year.

Coming a distant second was the continued strength of the Canadian dollar, with 19 votes, followed by the saga of former media baron Conrad Black and the demise of his Hollinger empire, with 14 votes.

Bay Street truly detests a surprise, and that became clear on Halloween when Finance Minister Jim Flaherty shocked the financial sector with a late-day announcement of new rules meant to put the brakes on the corporate shift towards income trust conversions.

Flaherty said such conversions amounted to tax avoidance on a grand scale. He declared that any new trusts will face regular corporate taxation while existing trusts get a four-year reprieve.

When markets reopened the next morning, panicky investors dumped their unit holdings, sparking a trust plummet on the Toronto Stock Exchange.

By Nov. 15, the income trust sector as a whole was down 14.3 per cent_ more than \$20 billion. By the end of December, it had recovered slightly to record a loss of about 10.5 per cent.

After the shock faded, the lobbying to change Flaherty's mind began. Not surprisingly, the most strenuous objections came from the trusts themselves.

In December, the Coalition of Canadian Energy Trusts released a report that supported their contention they should be exempt from new tax rules because they indirectly generate 30 per cent of the federal taxes produced by the oil and gas sector _ about twice as much as they represent in sector revenues.

The group plans to push its cause in the new year with the launch of a \$10-million "education" campaign.

Senior citizen investors said they were hit especially hard by Flaherty's decision. Income trusts have become a popular

RELATED STORIES

- ▶ [CP names Flaherty business newsmaker of year](#)
- ▶ [Whatever happened to the income-trust case?](#)
- ▶ [Ottawa: income trust reconversions to be tax-free](#)

USER TOOLS

[Print This Page](#)[E-Mail Story](#)[Feedback](#)Fonts: **Bigger** **Smaller**

investment for them because distribution payouts are generally higher and more regular than dividends from corporations.

Currently, cash distributions allow trusts to pay less tax than their corporate counterparts because they pass most of their taxable cash out to unitholders, who then pay income tax on what they receive.

Patricia Croft, chief economist and vice-president at Phillips, Hager and North, said in hindsight retail investors should've seen the decision coming because income trusts were simply too good to be true.

"I don't know that people had an understanding of the risk. They certainly enjoyed the benefit _ a very high yield _ but I think there was a view that they were a fabulous investment," she said.

"Most people thought of them as bonds, where the yield was secure. A lot of people didn't understand that risk, or the secondary risk that Ottawa would shut down the gain."

Investor advocate Diane Urquhart said seniors were often duped into viewing income trusts as a superior investment because of "inaccurate calculations."

"These products are being marketed to seniors and other unsophisticated retail investors on a basis of a measure called `fat cash yield,'" she said. "Seniors are being told they can earn more than double they can get from alternative investments like bonds and GICs."

Yet some seniors advocates have come to the defence of the Conservative government.

CARP, the Canadian Association of Retired People, commended Flaherty for "a prudent approach to his new policy regarding income trusts."

Though Flaherty has stood his ground, he has tried to make amends by offering "generous" rules that let existing trusts double in size over the next four years and convert back to public companies without taking a tax hit.

That likely means that the glory days of income trusts are over. A study released by accounting and consulting firm Deloitte predicted less than 50 income trusts will exist in Canada by 2011, when the rules are to be fully implemented.

Croft said reactions on Bay Street towards the Conservative government's decision have run the gamut.

"Some people say it was inevitable, and `Get over it and move on.' But there are others saying it wasn't fair, `You caught us completely off guard and went back on a campaign promise,'" she said, noting that the Conservatives initially pledged to avoid taxing income trusts after the Liberals floated the idea in 2005.

"In other jurisdictions around the world where changes have been made, often the time is five to 10 years. Canadians are only being given four years."

The Conservatives, meanwhile, have not remained unscathed. Some critics have suggested the trust changes could hurt the minority government's hopes of being re-elected.

Prime Minister Stephen Harper said the income trust decision was

the toughest decision the year-old government has had to make.

"It's not something we planned to do but it became apparent we had to do it. All neutral observers have concluded that," he told The Canadian Press in an interview.

Early signs that something was afoot arose earlier in 2006.

In the May budget, Flaherty raised the dividend tax credit on corporations in an effort to weaken the appeal of converting to a trust. Many suggested the effort was a careful step into territory that had hurt the Liberals less than a year earlier.

But those new rules didn't stop two of Canada's largest telecommunications companies, Telus (TSX:T) and BCE Inc. (TSX:BCE), from announcing plans in September to convert into trusts.

That put pressure on the government to take a stronger stance. By early October, Flaherty was telling reporters that the government would continue to watch the market.

A study released by tax expert Jack Mintz less than two weeks before the October announcement suggested the trusts would milk \$1.1 billion in tax revenue from Ottawa and the provinces _ double the \$540 million reported in 2004.

At the same time, analysts were predicting that grocery chains and mutual fund firms could be next in line to announce conversions.

Flaherty's announcement rattled those plans, causing a number of companies _ including Telus and BCE _ to back away from their conversion plans.

But the decision wasn't simply a move to protect government coffers, said Doug Porter, deputy chief economist at BMO Nesbitt Burns.

"I think they didn't want to see an income trust economy because their view is that income trusts don't do a lot of capital spending and it would harm long-term growth potential for the economy," he said.

"If they believed the tax leakage situation was going to remain static then they could've lived with it. It was concerns that it would turn into a tidal wave of conversions that was the ultimate trigger for them to act, and they acted decisively."

In the new year, said Croft, the trust sector will likely remain in flux, crunching numbers and "trying to figure out the what-if scenarios" for the future.

She said that includes determining which companies will return to a corporate structure and whether foreign investment and private equity will play a role in the sector.

"We're trying to sort through the debris and figure out where we go from here. I don't think we've seen a definitive resolution to this issue."

USER TOOLS

Print This Page

CANADIAN STORIES

► [Unemployment rate at 30-year-low in December](#)

[E-Mail Story](#)[Feedback](#)

- ▶ [More wild horses shot in Alberta, says group](#)
- ▶ [PM calls news conference amid defection rumours](#)
- ▶ [Bedard to appear in Quebec court Friday](#)
- ▶ [Ambrose out of environment post in cabinet shuffle](#)
- ▶ [N.S. minister resigns amid accident allegations](#)
- ▶ [Canada Revenue investigates botched mailout](#)
- ▶ [B.C. lawyer vindicated in Chretien pie plot](#)
- ▶ [Canada approves Relenza to prevent flu](#)

[About CTV](#) | [Careers](#) | [CTV Announcements](#) | [Advertise on TV](#) | [CTV Media](#) | [Advertise on Web](#)

[Archive Sales](#) | [Tapes and Transcripts](#) | [Privacy Policy](#) | [Terms and Conditions](#) | [Contact Us](#) | [Site Map](#)



© 2007 [CTVglobemedia](#) All Rights Reserved.
