

**WRITTEN BRIEF SUBMITTED BY**

**DYNAMIC VENTURE OPPORTUNITIES FUND LTD.**

**TO THE**

**HOUSE OF COMMONS STANDING COMMITTEE ON FINANCE**

**ON**

***BILL C-377***

***AN ACT TO AMEND THE INCOME TAX ACT (REQUIREMENTS FOR LABOUR ORGANIZATIONS)***

Dynamic Venture Opportunities Fund Ltd.

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ATTENTION: ROXANA TAVANA  
SECRETARY

## **1. INTRODUCTION**

On December 5th, 2011, the Honourable Russ Hiebert, Member of Parliament for South Surrey-White Rock-Cloverdale, moved for leave to introduce into the House of Commons *Bill C-377, An Act to amend the Income Tax Act (requirement for labour organizations)* (“**Bill C-377**”).<sup>1</sup> As stated in his submissions to the House of Commons, the purpose of this bill is to “amend the *Income Tax Act* to require the public disclosure of labour organization finances.”<sup>2</sup> Bill C-377, if enacted as currently proposed, would impose extensive new public reporting obligations on every “labour organization” and every “labour trust” as defined in Bill C-377.

## **2. SUBMISSIONS**

First, we respectfully submit that the *Income Tax Act* is not the appropriate vehicle through which to impose reporting requirements unrelated to tax liabilities or qualification for a particular status under the *Income Tax Act*. Accordingly, we would suggest that Bill C-377 should not proceed and should be abandoned.

Secondly, we respectfully submit that the proposed definition of “labour trust” in Bill C-377 is overly broad as it would have the unintended consequence of including prescribed labour-sponsored venture capital corporations, within the meaning of the *Income Tax Act* (“**LSVCC**”) within the proposed reporting requirements.

### 3. ANALYSIS

For the reasons outlined below, we submit that the proposed amendments to the *Income Tax Act* contained in *Bill C-377* should not be proceeded with or, in the alternative, that the proposed definition of “labour trust” should be amended to provide an explicit exception for LSVCCs.

- 1) Onerous Nature of the Proposed Bill. LSVCCs are already strictly regulated by securities, mutual fund, and tax legislation. This proposed additional regulation and reporting requirements will be extremely complicated, burdensome and expensive for LSVCCs and their sponsors who may decide to discontinue their support of LSVCCs due to the onerous reporting requirements associated with their sponsorship of LSVCCs. We respectfully submit that the cost benefit analysis of such additional disclosure also points to the fact that while the LSVCCs and their sponsors will be required to expand significant additional human and financial resources in order to gather and prepare the required information, the incremental value of providing such information to the public will be minimal. Such additional costs may also affect the overall profitability of LSVCCs and their unitholder value.
  
- 2) Confidentiality Concerns. The proposed amendments, if implemented, will require unnecessary public disclosure of confidential information for LSVCCs which operate in a competitive commercial environment for both investments and investors. For example, the requirement of detailed reporting of all transactions over \$5,000, the names of the parties to such transactions and their personal information (where individuals are involved) would required that LSVCCs divulge information which is currently protected

not only by the legislation (in case of individuals) but also by contractual obligations between LSVCCs and its third party service providers. Third party providers may refuse to enter into arrangements with LSVCCs as their competitive information (such as pricing) will need to be disclosed. It is likely that due to the above, LSVCCs may no longer be able to obtain the necessary products and services from their third party providers at competitive prices as such providers will either refuse to enter into transactions with LSVCCs (in order to protect their own competitive information) or charge an additional premium on the delivery of such services.

- 3) Inconsistency. The imposition of the proposed reporting requirements contained in Bill C-377 on LSVCCs is both unnecessary and inconsistent with the stated objective of Bill-377 “to require the public disclosure of labour organization finances” as none of the economic benefits of an LSVCC can accrue to a labour union.

We respectfully submit that the proposals in Bill C-377 should not be proceeded with. In the alternative, we respectfully submit that the definition of “labour trust” as proposed in clause 1 of Bill C-377 should be amended to specifically exclude “prescribed labour-sponsored venture capital corporations” as defined in the *Income Tax Act*. Suggested wording for the definition of “labour trust” is presented below in the section entitled “Summary of Recommendations.”

## **2. ORIGINS OF LSVCCs**

LSVCCs, also known as labour-sponsored investment funds, are funds managed by investment professionals that invest primarily in small and mid-sized private companies. As the name suggests, an LSVCC must be “sponsored” by a labour union.

The first LSVCC program was introduced in Quebec in 1983.<sup>3</sup> At the time Quebec was emerging from a recession. The lack of capital in small and mid-sized companies had caused numerous bankruptcies. Labour leaders in Quebec had been concerned by permanent employment losses, plant closures, and production and investment relocation during the recession. As a result they were of the view that labour should be more directly involved in the capital markets. The Quebec government proposed a “solidarity fund” to help the province create a locally-controlled healthy and sustainable economy. The underlying objective was to create an incentive for attracting venture capital to smaller Quebec firms. The federal government soon followed suit and introduced similar rules into the *Income Tax Act*. A number of provinces also introduced their own LSVCC regimes (notably Saskatchewan, British Columbia, Manitoba, Ontario, Nova Scotia and the Northwest Territories). Dynamic Venture Opportunities Fund Ltd. is an LSVCC established pursuant to the *Ontario Community Small Business Investment Funds Act, 1992*.

## **3. REGULATION OF LSVCCs**

As investment funds, LSVCCs are highly regulated in Canada by provincial securities laws, and provincial and federal income tax authorities. The *Income Tax Act* defines the “registered labour-sponsored venture capital corporation” as “a corporation that was registered under subsection 204.81(1), the registration of which has not been revoked.”<sup>4</sup> Subsection 204.81(1) establishes the

conditions for registration of a corporation as a LSVCC. These conditions are based on the strict observance of corporate, securities and mutual funds legislation.<sup>5</sup> The Ontario *Community Small Business Investment Funds Act, 1992*, as well as the other provincial regimes, impose similar requirements on LSVCCs subject to those regimes.

Moreover, LSVCCs are also subject to the regulation and reporting requirements for mutual funds or investment funds under provincial securities laws. These include continuous disclosure obligations the intent of which is to require financial transparency.

#### **4. INVOLVEMENT OF LABOUR UNIONS IN LSVCCS**

In order to qualify as an LSVCC under the *Income Tax Act* (the Ontario *Community Small Business Investment Funds Act, 1992* imposes similar requirements) a fund must have two classes of shares, being Class A shares and Class B shares, the terms of both of which must satisfy the requirements of the *Income Tax Act*. As well, the Class A shares must be issuable only to individuals (other than trusts) and to trusts governed by registered retirement savings plans (“RRSP”) or tax free savings accounts (“TFSA”). Class B shares must be issuable only to and may held only by “eligible labour bodies” (or, in the case of the Ontario rules, “employee organizations”), which are defined to mean only certain labour unions and related organizations. Class B shares are not permitted to receive dividends from the LSVCC and the holder of such shares is only entitled, on the dissolution of the LSVCC, to the amount originally received by the LSVCC upon the issuance of the shares (in other words, the labour union holder of the Class B shares is entitled only to receive a return of its invested amount and will not derive any appreciation or gain on its investment). The rights of the holder of the Class B shares are

essentially limited to receiving notice of meetings of the shareholders of the LSVCC. An LSVCC may not issue any further classes of shares except with the specific approval of the Minister of Finance.

## **5. SUMMARY OF RECOMMENDATIONS**

On behalf of Dynamic Venture Opportunities Fund Ltd., we respectfully submit that the proposed changes to the *Income Tax Act* contained in Bill C-377 are inappropriate and should not be proceeded with, and that Bill C-377 should be abandoned. As noted above, the reporting requirements proposed in Bill C-377 have nothing to do with tax reporting, either in terms of the tax liability of particular taxpayers or in terms of the tax status of any particular taxpayer or entity. Accordingly, they should not be included in the *Income Tax Act* and Bill C-377 should not be proceeded with.

If, notwithstanding the arguments above, it is decided that Bill C-377 should, in general terms, proceed, we submit that the proposals, in particular the proposed definition of “labour trust”, are overly broad as they would have the unintended consequence of including LSVCCs within the proposed reporting requirements. As noted above, LSVCCs are already strictly regulated by securities, mutual and investment fund, and tax legislation and subject to extensive and continuous disclosure obligations and financial transparency. The proposed additional regulation and reporting requirements will be extremely complicated, burdensome and expensive for LSVCCs. Moreover, they will require unnecessary public disclosure of confidential information for LSVCCs which operate in a competitive commercial environment for both investments and investors.

Accordingly, if Bill C-377 is proceeded with, then we submit that the Honourable Members of the House of Commons Standing Committee on Finance should amend the definition of “labour trust” in *Bill C-377, An Act to amend the Income Tax Act (requirements for labour organizations)* by including the following underlined wording:

149.01 (1) The following definitions apply in section 149 and in this section.

...

“labour trust” means a trust or fund, other than a prescribed labour-sponsored venture capital corporation, in which a labour organization has a legal, beneficial or financial interest or that is established or maintained in whole or in part for the benefit of a labour organization, its members or the persons it represents.

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<sup>1</sup> Bill C-377, *An Act to amend the Income Tax Act (requirements for labour organizations)*, 1st Sess, 41st Parl, 2011 (as referred to Committee on 14 March 2012).

<sup>2</sup> *House of Commons Debates*, 41st Parl, 1st Sess, No 60 (5 December 2011).

<sup>3</sup> Duncan Osborne & Daniel Sandler, “A Tax Expenditure Analysis of Labour-Sponsored Venture Capital Corporations” (1998) 46:3 Can Tax J 499.

<sup>4</sup> *Income Tax Act*, RSC 1985, c 1 (5th Supp), s 248(1) “registered labour-sponsored venture capital corporation”.

<sup>5</sup> *Ibid*, s 204.81(1).