

Fiscal and Economic Impact of Canada's Labour-Sponsored Investment Funds: Findings Related to Fair Exchange Concept

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Labour-Sponsored Investment Funds Concept

- Canada's federal and most provincial governments subsidize the Funds through tax credits.
- Tax credits provided to ordinary taxpayers (15%+15%).
 - Objective is to raise funds to fill an alleged shortage of venture capital faced by small and medium-sized business.
 - Labour unions or labour federations sponsor the creation of the Funds, with varying control of Board/management .
 - Taxpayers are the owners, unions are the sponsors
- Tax credits go directly to owners (taxpayer shareholders), indirectly to businesses that receive the venture capital

Who participates in these Funds?

- From a shareholder standpoint, they are ordinary taxpayers.
In recent study, 22% of investors had incomes below US\$32,000 and 48% below US\$48,000, close to the median taxfiler income level in province that was studied (Ontario).
30% paid union dues or professional fees.
- Taxfiler LSIF investments intended for retirement income.
i.e. to improve post-retirement incomes = 60% of pre-retirement. Most are sheltered in RRSP (Canada's IRA).
- From an investee standpoint, small business are the participants. In the Ontario, 68% had fewer than 50 employees, 32% were start-ups

What type of study did we do?

- Prepare estimates of subsidy cost
- Prepare estimates of what do taxpayers receive as benefits – jobs and economic growth for citizens, revenues for their governments
- Studies were done for LSIFs in 3 provinces
- Ontario study is illustration that follows

Objective of Ontario Study

- to estimate the costs to Ontario and federal governments of labour-sponsored funds (LSIF) legislation and the economic and fiscal benefits
- this analysis deals only with Ontario Funds that are members of Association of Labour Sponsored Investment Funds – ALSIF – nine Funds participated in study – invested up to year 2001 about US\$1.6 b. Economic impact measured in 2002.

How to estimate fiscal costs

- simulate the tax returns of shareholders, as they purchase shares and after retirement
- do the simulation twice -- under existing legislation and again if LSIFs did not exist
- the difference is the fiscal cost of LSIFs
- there are some offsets to the tax credits, e.g. consumption taxes, higher retirement tax revenues => net cost < 15% tax credit

How to estimate benefits

- obtain data on the growth of investees after ALSIF Funds made their investments
- estimate how much of the growth could be attributed to the Fund's investment
- submit the totals to University of Toronto econometric model
- simulate impact on economy of Ontario and Canada and revenues to each government

How to attribute investee growth to the LSIF investment(s)

- determine company size before LSIF investment was first made and then after (2002)
- estimate portion of growth attributable to project
- estimate portion of growth captured from Ont. competitors
- pro-rate growth based on LSIF financing share
- survey investees on what would have happened without existence of LSIF
- benefit estimates are conservative

Highlights of Investee Performance

- Sample of 185 investees
- The firms performed extremely well. Here are before and after results – pre-investment year vs. 2002:
 - exports: 109 firms - \$515m. before >> \$2b. in '02
 - R&D: 116 firms - \$175m. before >> \$700m. in '02
 - direct jobs: 9,000 before >> 31,800 by 2002
 - payroll: \$430 m. before >> \$1,800 m. by 2002

Impact on the Economy

- if LSIFs did not exist, Ontario's economy would have been this much smaller in 2002:
 - * GDP: \$2.3 b.
 - * Employment: 27,000
 - * provincial revenues: \$357 m.
 - * federal revenues: \$449 m.
 - * future incremental revenues will be higher, because most investees are growing firms

What Fair Exchange did the Public receive?

• Ontario

- * cost from inception to 2000: \$494 m.
- * benefit in 2002: \$357 m.
- * payback: 1.4 years
- * net revenues 2003 onward
- * 27,000 more jobs
- * more residents able to start/grow their companies

• Canada

- * cost from inception to 2000: \$489 m.
- * benefit in 2002: \$449 m.
- * payback: 1.1 years
- * net revenues 2003 onward