



FAQ: Flow-through Shares (FTS)

Why does the Government of Canada provide investors with a flow-through tax deduction?

The Government of Canada has recognised the economic benefits of supporting the exploration for, and development of, Canada's natural resources. In recent years, the federal government and some provinces have introduced additional investment incentives for Canada's mining industry.

How do FTS work?

The FTS program allows the issuing corporation to transfer exploration and development expenses to the investor in the form of tax deductions. The FTS must be newly issued shares that have the attributes generally attached to common shares.

Companies must spend the proceeds on qualifying exploration and development expenditures in Canada. These expenses are subsequently "flowed-through" or passed from the company to the investor:

- the investor is able to deduct the renounced expenditures against other income thereby effectively reducing the risk of investment;
- the company cannot expense or amortize expenditures that have been renounced to investors;
- and the tax cost of the investor's FTS is reduced to zero.

Who can purchase FTS?

Canadian taxpaying entities are permitted to purchase FTS. This includes individuals, trusts, corporations, and partnerships.

What companies can issue FTS?

A corporation whose principal business involves specific activities related to the oil and gas, mining, renewable energy, or energy conservation sectors can issue FTS.

When was the FTS program introduced?

The federal government introduced a FTS program for Canada's resource sector in 1954 and extended it to certain aspects of renewable energy technologies (particularly wind power) in the mid 1990s.

Why are FTS attractive to investors?

Investors purchase FTS, at a premium, in exchange for a significant tax benefit. Several provinces including Ontario, British Columbia, Manitoba, Quebec, and Saskatchewan offer additional flow-through deductions, making the tax incentives to purchasing FTS even more attractive.



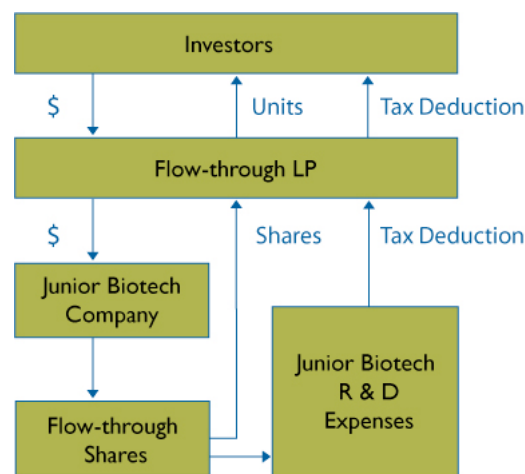
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Does an investor have to invest directly into a company?

An investor has two options to invest in FTS:

1. Invest directly in a company, or,
2. Invest in a limited partnership (LP) with aggregate investments from many investors. The LP pools the funds and subsequently invests the funds in several FTS issuers. Figure 1 is a graphical depiction of an investment in a flow-through LP.

Figure A: Investment in a Flow-Through Limited Partnership

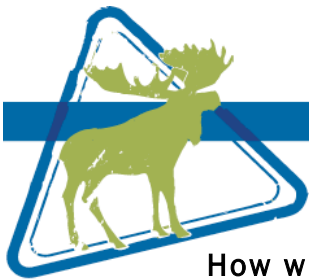


Why do junior resource companies, in particular, benefit from FTS?

Junior resource corporations often have difficulty raising capital to finance their exploration and development activities. Moreover, many are in a non-taxable position and do not need to deduct their resource expenses. The FTS mechanism allows the issuing company to transfer the resource expenses to the investor in the form of a tax deduction thereby conferring a tax-benefit to the investor. Junior resource corporations are the primary corporate beneficiaries from FTS financing in Canada.

How do investors sell their FTS?

- 1) Investments in the FTS of public companies are converted to common shares sometime after issuance, thereby becoming normally traded shares on a public exchange.
- 2) Investments in the FTS of private companies are usually transferred eighteen to twenty-four months from the close of a limited partnership offering by way of a tax-deferred rollover of the limited partnership's assets to a mutual fund. Investors can then choose to either hold or sell the mutual fund units.



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How will FTS help the lack of available venture capital in Canada?

Public risk capital can be a complement to traditional venture capital. Demonstrated success in the resource sector has shown the lack of traditional capital can be restored by enticing high-net worth investors to invest in high-risk projects.

How do you ensure there is little or no program abuse?

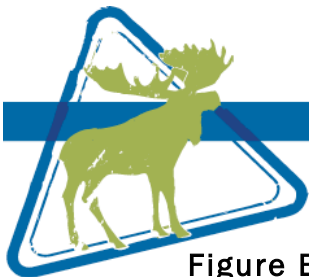
The Canada Revenue Agency (CRA) has risk-control mechanisms in place to minimise program abuse. Market forces are at work ensure the cost of capital is reasonable. The only other source of potential abuse could be fraud by the issuing company not investing the proceeds as required, in which case the tax benefit to the investor would be denied and civil suits would likely follow.

Do FTS attract international investors?

The combination of FTS financing and the prestige of the Toronto Stock Exchange has created a tremendous amount of visibility for Canada's natural resource sector. The experience of Canada's resource sector indicates global capital has found opportunities in this sector.

What are the results of the FTS program?

The FTS program has helped position Canada as a primary destination for international resource companies and as a global leader in natural resource financing, and has been a significant factor in kick-starting Canada's clean-technology sector. Figure B presents several economic growth factors in the natural resource and clean-technology industries.



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Figure B: Impact of FTS – Growth of Natural Resource and Clean-Tech Industries in Canada

RESOURCES		CLEAN-TECHNOLOGY
Oil and Gas	Mining	
<ul style="list-style-type: none"> • Economic impact to Canada’s GDP estimated at \$3.56 trillion over the last 25 years. • Federal and provincial tax revenues total \$1.1 trillion over the last 25 years. • Canada is home to the largest number of publicly-traded oil & gas issuers (385) in the world. • Canada’s public markets are home to over 35% of the world’s public oil and gas companies. • More than 40 analysts cover oil and gas companies listed on Canada’s public markets. 	<ul style="list-style-type: none"> • A record \$22.2 billion was raised on the TSX and TSX-V by listed mining companies in 2009. Canada’s capital markets are now the global leader in resource finance. • Approximately 60% of the world’s mining exploration companies are Canadian. • Over 1400 Canadian and international mining companies are listed on Canada’s public exchanges and 50% of these companies’ mineral exploration projects are held outside of Canada. • More than 20% of worldwide exploration expenditures take place in Canada. • Canadian mining companies engage in more exploration projects than companies from any other country. • Over 200 analysts cover mining companies listed on Canada’s public markets. 	<ul style="list-style-type: none"> • Toronto Stock Exchange and TSX Venture Exchange are home to the highest number of clean technology companies (125) in the world. • In 2009, Canada’s clean technology and renewable power companies raised over \$1.5B through the public markets, and have experienced a CAGR of 35% in trading volume between 2005 and 2009. • More than 30 analysts cover publicly-traded Canadian clean technology and renewable power companies.

Sources: Toronto Stock Exchange, Canadian Mining Association, Canadian Association of Petroleum Producers, Natural Resources Canada, Metals Economics Group

Are there other sectors that could benefit from the FTS program?

The program is attractive to industries requiring significant resources to finance capital-intensive projects and whose expenditures are not needed to offset revenues (as revenues are uncertain and remote). Canada’s junior biotechnology companies accumulate and carry-forward multi-millions of dollars of tax losses, incurred as a result of R&D projects, every year. High R&D intensive industries, such as Canada’s biotechnology sector, can benefit from the FTS program.

Why are FTS particularly attractive for life sciences companies?

Like the resource sector, the life sciences sector is modeled on the premise of discovery and commercialisation, reliant on large amounts of high-risk, venture capital where revenues are uncertain and remote. Bringing a therapeutic drug to market can take up to 15 years and cost more than \$1 billion. The vast majority of life sciences firms are typically not profitable and as such, carry-forward a tremendous amount of tax losses yearly. Canada’s venture capital industry is too small to completely fund these needs; FTS filled the funding gap for the resource sector by providing risk capital at higher values through the public markets.

How will FTS stimulate other investments in the life sciences sector?

The track record of the resource sector shows FTS made capital that could not otherwise be accessed available to companies, and, in turn, generated additional non-FTS capital.



Biotechnology companies already get SR&ED tax credits. Why should they be able to issue FTS?

The SR&ED tax credit program is an *ex post* source of capital. The availability of risk capital is an essential element to financing R&D projects. The SR&ED tax credit is not of value to companies unless risk capital is available for companies to finance their R&D projects and claim SR&ED eligible expenses. In addition, the SR&ED program's CCPC restriction against refundable tax credits does not permit publicly-traded and other non-CCPCs biotechs to benefit from the SR&ED tax credit program. The FTS program is an alternative method for these companies to raise capital.

How will expansion of the FTS program to the biotechnology industry benefit the Canadian economy?

Expanding FTS to the biotech sector results in a number of economic gains to the Canadian government, the business sector, and the overall economy. Expanding the FTS shares program to junior biotechnology companies is estimated to result in more than \$400 million in incremental R&D. This, in turn, is expected to generate nearly \$1 billion in gross output, more than \$500 million in GDP gains, and create nearly 8,000 new jobs. The federal government also recoups incrementally more capital gains taxes, as the adjusted cost-base of every FTS purchase is set to zero, implying incremental capital gains tax revenues that would not have otherwise occurred for the treasury, even when shares are sold at a loss.