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Canadian Institute for Environmental Law and Policy  
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Conservation of Natural Heritage

# Incentive Proposals for Endangered Species on Private Lands

**Discussion Paper prepared for the  
National Round Table on the Environment and the Economy**

**Economic Instruments to Encourage Sustainability on  
Private Lands Workshop**

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by

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This report is prepared for general discussion purposes only. Any interpretations errors or omissions are the sole responsibility of the author. The report is not intended to provide legal or financial advice and any specific taxation questions should be discussed with appropriate legal, financial or other advisors.

## Introduction

Canada has a growing number of 268 species at risk (i.e. vulnerable, threatened and endangered), not including those 23 species which have disappeared entirely. The growing list of species at risk is due to a variety of factors, with the single largest factor being the loss of habitat - where the species lives.

The shrinking numbers of these species have an effect on people in numerous ways, including the potential loss of: our natural heritage and relationships with the land; future medicines and agriculturally-valuable genetic material; ecological services; and early warning systems of environmental changes that may eventually threaten humans. Direct economic benefits also arise from retaining a diversity of species, whether common or near extinction. In 1991 for example, Canadians spent approximately \$8.2 billion on wildlife-related activities, generating over 200,000 jobs and \$2 billion in tax revenues used for numerous programs.<sup>1</sup>

Except in the Territories, the federal government owns only a tiny portion of Canada's land area, while provincial governments have extensive holdings in most provinces. In contrast, just 10 percent of Canada is held in private hands. Throughout the country, forestry occurs on 24%, agriculture on 7%, and urban and industrial uses on just 1% of the total land area. Six percent of forest land in Canada is held in private hands. Analysis has shown that, of 243 listed species at risk in 1995, only 17 (or 7%) are significantly affected by agricultural activities.

While the statistics for private lands, intensive land uses and numbers of species affected by agriculture may be small, location and associated politics are much more significant. Private lands are found largely in the southern parts of the country, where biodiversity, human populations, arable soils, easily accessible resources and consequent conflicts are greatest. On these southern and largely private lands, the landscape has been transformed and parcelled out in order to develop Canada's diverse communities and world-renowned agricultural and wood products. However,

this has also left less room for and caused more significant impacts upon wild plants and animals.

Private land owners and managers include farmers, ranchers, forestry and mining companies, and residential and recreational property owners. Each has a different relationship with and use of the land and the resources it provides, and some have the opportunity and many have the willingness to help species at risk. Given the right incentives and a sense that the burden is shared, more private landowners and managers will want to and be able to contribute in our collective efforts to prevent species from disappearing.

In numerous ways over the years, Canada has committed to protecting and developing legislation for species at risk. Among others, these commitments include: ratification of the international *Convention on Biological Diversity*; leading development of and signing of the *Canadian Biodiversity Strategy* and "National Accord for the Protection of Species at Risk"; the 1993 and 1997 "Red Book" election platforms of the governing Liberal Party; and the public announcements of a succession of federal Environment Ministers. Support for legislation that protects endangered species and their habitat has also been expressed by scientists, churches, and labour, agricultural and environmental organizations across Canada.

A major step towards implementing these commitments occurred with the introduction of the *Canada Endangered Species Protection Act* (Bill C-65, or "CESPA") in late 1996, following considerable public consultation and the advice of the Federal Endangered Species Task Force. Attempting to avoid provincial jurisdiction over property matters, the largely regulatory measures seemed to affect private lands in a fairly limited manner. While the Bill was not passed before Parliament was prorogued for an election, it may be revived in some form during the new mandate.

Over the years, a number of federal government initiatives have addressed species at risk. These initiatives have included: early passage and more recent

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<sup>1</sup> See F.L. Filion, E. DuWors, P. Boxall, P. Bouchard, R. Reid, P. Gray, A. Bath, A. Jaquemot, and G. Legare, *The Importance of Wildlife to Canadians: Highlights of a Survey* (Ottawa: Canadian Wildlife Service, 1993).

amendments to the *Migratory Birds Convention Act* and *Canada Wildlife Act*; establishment and secretariat functions for the scientific Committee on the Status of Endangered Wildlife in Canada (COSEWIC) and Recovery of Nationally Endangered Wildlife (RENEW); and a variety of habitat and ecosystem restoration programs which have incorporated species at risk considerations, including enhanced income tax benefits for donations of "ecologically sensitive lands" to charities and municipalities.

Many of these initiatives have recognized the role of voluntary stewardship, and have incorporated some form of economic incentive. However, given the growing numbers of species at risk, these measures are not sufficient. Consequently, more needs to be done to respond to landowner concerns and to develop stewardship measures as part of a comprehensive package to protect species at risk in Canada. As the federal government is considering its options and proceeding with its budget development process, the following proposals are submitted for discussion, refinement and implementation. In particular, they attempt first to recognize conservation investments made by private landowners, and second to leverage new and non-governmental funding and land donations in order to conserve our most threatened wildlife and the habitat essential for its survival. Many of the measures are cast to benefit all wildlife, but will nonetheless benefit and can be focused towards those species most at risk.

## **A. Credit Farmers and Woodlot Owners for Conservation Investments**

### **Background**

As determined by courts over the centuries, wildlife is generally considered Crown (or government) property until legally captured or killed, while vegetation is owned by the owner of the land on which it grows. This then creates the need for a partnership between landowners and government, and between federal and

provincial levels and responsibilities, in order to manage and conserve both wildlife and its habitat.

Farmers and woodlot owners play significant roles in conserving the habitat of species at risk on private lands, and they receive a variety of income tax benefits for investing in their businesses. Unfortunately, some expenses or losses incurred when they invest in conservation practices produce no immediate, and at times no long-term, recognition in our tax system. If such expenses were recognized for specified purposes, including the protection of endangered species habitat, then farmers and woodlot owners would be more inclined to make such investments, and would share not only the benefits but also the costs of such investments with the general Canadian public.

In the rest of this section, woodlot owners will be lumped into the term "farmer", since they are all treated more or less the same under the *Income Tax Act* (ITA). This is because people planting and growing trees on their lands for eventual harvest and sale in an expectation of profit, and who are not otherwise engaged in a lumbering or logging business, are considered for tax purposes to be farmers by Revenue Canada.<sup>2</sup> While this section focuses upon farmers and woodlot owners, the incentives proposed here for rewarding conservation investments may also be adaptable to other sectors, in appropriate circumstances.

The types of investments farmers might make to conserve endangered species habitat can be clustered into three categories: new or improved equipment; extended operation of equipment (e.g. avoiding sensitive habitat); and planting and tending appropriate vegetation (trees, food or cover crops, etc.). Under the ITA, expenses incurred for these types of investments are treated in different ways, as described below.

New or improved equipment may include fencing along streams or to protect crops, tractors with wider tires to reduce compaction, harvesting equipment with higher cutting levels or bars to flush waterfowl, or

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2 *Farm Woodlots and Tree Farms*, Interpretation Bulletin IT-373R (Ottawa: Revenue Canada Taxation, 14 March 1985), para.7. Note that Revenue Canada recognizes three categories of farming, with varying eligibility for deductions. Many woodlot owners would be considered part-time farmers, and thus would have "restricted farm losses".

fishing nets with coarser openings. For tax purposes, new or improved equipment is classified into different classes of "depreciable property", and farmers can deduct a specified percentage of its cost each year (the "capital cost allowance" or CCA) from income, and add improvement-related expenses to the value of such depreciable property. If the CCA percentage is small (often because the lifespan of the equipment is long), there is less of an incentive to buy such equipment, since more of the expense will be deductible in future years.

If new equipment is used solely to stop, reduce, or eliminate air or water pollution, such equipment may qualify for an accelerated capital cost allowance rate as an incentive.<sup>3</sup> There is also an investment tax credit available, up to annual limits, to recover a certain percentage of qualifying expenditures, particularly for scientific research and experimental development purposes (including applied research), and subject to restrictions that preclude many conservation applications.<sup>4</sup> The Canadian Federation of Agriculture recently passed a resolution supporting a tax credit for equipment that enhances land and wildlife conservation (such as that for no-till or wildlife flushing operations).<sup>5</sup>

Increased operating expenses from extended operation of machinery to protect wildlife (e.g. fuel, oil, repairs, licences, and insurance), as well as general expenses applicable to the combined farmed and unfarmed

property (e.g. gear, small tools, telephone, memberships, property taxes, office expenses and accounting), can be deducted from current-year income, and any losses can be carried over and used in any three past or ten future years. This means that such extra costs to conserve species at risk, and any expenses incurred in raising crops that are later destroyed by wildlife, will be deductible. As discussed below, Revenue Canada may disallow such operating and general expenses in proportion to the extent that lands for wildlife are not used for a farming business, but only for personal purposes or as a capital investment.<sup>6</sup> If farming or farming in combination with other sources is not the taxpayer's chief source of income (e.g. for a woodlot owner), then losses resulting from these expenses may be treated as "restricted farm losses" usable as deductions in other years only against farm income, or may even be ineligible for deduction purposes.<sup>7</sup>

The tax treatment of the planting and care of vegetation for wildlife conservation purposes is somewhat complex. Where a farm earns either minor or significant income from a woodlot, wood product sales are considered farming income and replanting costs are deductible from such income.<sup>8</sup> This will only be the case when the operations are carried on with a reasonable expectation of profit (e.g. to cut and sell the timber), otherwise they will be disallowed because they are "personal or living expenses" or are not incurred to

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3 *Capital Cost Allowance - Pollution Control Property*, Interpretation Bulletin IT-336R (Ottawa: Revenue Canada Taxation, 9 January 1985). This incentive is not intended to apply to equipment acquired after 1998.

4 ITA, ss. 37(1) and 127(5); see *Investment Tax Credits*, IT-331 (Ottawa: Revenue Canada); and *Scientific Research and Experimental Development Expenditures*, IT-151R4 (Ottawa: Revenue Canada, 16 August 1993) and IC-86-4R3 (Ottawa: Revenue Canada, 24 May 1994).

5 Canadian Federation of Agriculture, Annual Meeting, February 1997; personal communication, Sally Rutherford, Executive Director, 26 September 1997.

6 However, the wooded, groundwater, non-arable and arid portions of a farm should be considered part of the farm, and not segmented and excluded for the tax treatment of a farm transfer to a child: *Bouchard Estate v. Minister of National Revenue* (1993), [1993] 2 C.T.C. 3003, 93 D.T.C. 1511 (Eng.) (T.C.C.).

7 ITA, s.31; *Farm Losses*, Interpretation Bulletin IT-322R (Ottawa: Revenue Canada, 25 October 1978); *Losses - Deductibility of Restricted Farm Losses, Non-Capital Losses and Net Capital Losses*, Interpretation Bulletin IT-232R2 (Ottawa: Revenue Canada, 30 December 1987).

8 IT-373R, cited above, paras. 2 to 6.

gain income.<sup>9</sup> The courts have held that a systematic or organized program or plan is an important factor in finding such an expectation of profit.<sup>10</sup> Planting of other vegetation besides trees would likely receive similar treatment.<sup>11</sup> Of less interest to farmers, landscaping expenses paid by taxpayers around the buildings they own and use for producing income or for a business are also deductible against current-year income; these must be conducted largely for aesthetic and beautification purposes, rather than for utility alone.<sup>12</sup>

Where trees or other vegetation are not planted for harvesting in the expectation of profit or for the landscaping of grounds, they may nonetheless enhance the value of the property (e.g. future harvesting, presence of wildlife, recreation, aesthetics, wind and erosion protection, water retention, soil structure and productivity). In this case, expenses for planting, fertilizing and thinning etc. could be treated as capital expenditures and added to the total costs of the land, thereby reducing capital gains and associated tax when the property is transferred. However, this benefit may occur many decades into the future when the farm is

eventually sold or inherited; it does not provide immediate credit or reinforcement to the farmer, and the present value of such benefit will often be negligible, thus discouraging such investments. With a lifetime capital gains exemption of \$500,000 for qualified farm properties, such investments may receive no distinct recognition or benefit at all.

In contrast to such limits on making habitat investments, Section 30 of the *Income Tax Act* provides that amounts paid "for clearing land, levelling land or installing a land drainage system for the purposes of the [farming] business" are deductible from farming income. This includes clearing the land of brush, trees, roots, stones etc., the initial ploughing in order to put the land into productive use, and laying tile drainage.<sup>13</sup> Where such an amount is deductible, this amount is excluded from the cost of depreciable property and claims for capital cost allowance on such property.<sup>14</sup>

The problem, then, is how to provide tax benefits to farmers and similar land managers for appropriate equipment and habitat improvements, and ensure that tax benefits are not available for certain habitat-destroying activities.

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9 IT-373R, cited above, para.1; ITA, paras. 18(1)(a) and (h). In s. 248(1) "personal and living expenses", this term is defined to include "the expenses of properties maintained by any person for the use or benefit of the taxpayer" or a relative, "and not maintained in connection with a business carried on for profit or with a reasonable expectation of profit". Numerous court cases have disallowed deductions for tree planting because there was no reasonable expectation of profit, for example: *Madronich v. Minister of National Revenue*, [1984] C.T.C. 2319, 84 D.T.C. 1300 (T.C.C.); *Jourdenais v. M.N.R.* (1987), 87 D.T.C. 440 (T.C.C.); *Roy v. M.N.R.* (1987), 88 D.T.C. 1275 (T.C.C.).

10 In *April v. Minister of National Revenue* (1982), [1982] C.T.C. 2083, 82 D.T.C. 1092 (T.R.B.), a physician fenced his property in order to feed and hunt deer, and through a government program planted trees with intentions to cut them. While the Board found that the "care and upkeep of wild animals may also under certain conditions be referred to as farming", there was no evidence that the expenses claimed were part of an "organized and systematic program" for earning a profit. See also: *Gagnon v. M.N.R.* (1985), 85 D.T.C. 493 (T.C.C.); *Dell v. M.N.R.* (1984), [1984] C.T.C. 2425 (T.C.C.); *Mannella v. M.N.R.* (1984), [1984] C.T.C. 3046, 85 D.T.C. 19 (T.C.C.); *Morisset v. M.N.R.* (1984), 84 D.T.C. 1176 (T.C.C.).

11 Also see *Income Tax Regulations*, C.R.C. 1978, c.945, s.1702(1)(f), (g) and (h), where deductions for capital cost allowances are not allowed for property that: was not used in the farming business during the year; is an animal or a tree, shrub, herb or similar growing thing [emphasis added]; or was not acquired by the taxpayer for the purpose of gaining or producing income from farming or fishing. These regulations only apply to properties held continuously since before 1972.

12 ITA, para.20(1)(aa); *Landscaping of Grounds*, Interpretation Bulletin IT-296 (Ottawa: Revenue Canada, 1 March 1976).

13 *Cost of Clearing or Levelling Land*, Interpretation Bulletin IT-485 (Ottawa: Revenue Canada, 19 April 1982), para.8.

14 *Ibid*; *Income Tax Regulations*, C.R.C. 1978, c.945, ss. 1102(1)(a) and 1702(1).

## Proposals

The author proposes that there be amendments to the *Income Tax Act* and its Regulations to implement the following:

1. Disallow costs of clearing or levelling land, unless an appropriate agency has either exempted the property or such clearing or levelling is carried out in accordance with an approved conservation or restoration plan. The application of this measure could be limited in its geographic scope by designating areas where it would (or would not) apply.
2. Enable expense deductions against current-year income of costs paid for plan preparation, specific conservation or environmental mitigation equipment, and the improvement of habitat for wildlife, where there is a conservation or restoration plan approved by an appropriate federal, provincial or other agency. Ideally, these deductions would be without restriction on amount or period of carry forward, but, if necessary, the initiative could be made subject to certain caps, thresholds, documentation or non-reimbursement requirements, time limits or percentages of area or income, and could be limited to the habitat of species at risk.

Consideration may also be given to alternatives to number 2 that would somewhat modify and become integrated into existing programs, as described below.

- 2B Treat all such expenses as deductible or creditable donations to the Crown for the purposes of protecting Crown interests in wildlife.
- 2C Enable investments in equipment and land management under an approved conservation or restoration plan to qualify for full investment tax credits.

- 2D Create a new conservation class of depreciable property with a substantial percentage of capital cost allowance for fences, other structures, and equipment built, improved or acquired as part of an approved conservation or restoration plan.
- 2E Enable fences or other structures erected or improved as part of an approved conservation or restoration plan to be included as pollution reduction equipment, and thus be eligible for an accelerated rate of capital cost allowance.

## Examples

A number of domestic examples exist of comparable approaches, particularly for the second proposal. As noted above, the costs of landscaping around buildings for aesthetic purposes are deductible, even though such costs would otherwise be considered capital expenditures that would have no immediate taxpayer benefit. The fencing aspect of this proposal is consistent with Environment Canada's accelerated capital cost allowance for pollution control property, since fences can significantly reduce non-point sources of pollution by keeping cattle out of streams, and conservation of endangered and threatened species is at least of equal importance and urgency as pollution control. The Medical Expense Tax Credit provides a credit for expenses and devices based on the lowest tax bracket percentage multiplied by the lower of a) expenses incurred above a specified cost, or b) 3 percent of net income; such expenses must be proven by filing receipts and must not have been reimbursed or reimbursable.<sup>15</sup> The Minister of the Environment, or the Minister's governmental or non-governmental delegate, also undertakes a certification process for donations of "ecologically sensitive lands" in order for enhanced tax benefits to apply.<sup>16</sup> Donations to the Crown are deductible for corporations, and qualify for tax credits for individuals.

<sup>15</sup> ITA s.118.2(1); *Medical Expense and Disability Tax Credits and Attendant Care Expense Deduction*, Interpretation Bulletin IT-519R (Ottawa: Revenue Canada, 20 February 1995), paras. 12-18.

<sup>16</sup> Canadian Wildlife Service, *Donation of Ecologically Sensitive Land in Canada: Implementing New Provisions of the Income Tax Act of Canada*, Revised Information Circular No. 2 (Ottawa: Canadian Wildlife Service, 1997).

The *Farm Bill* introduced similar measures into the United States *Internal Revenue Code* (IRC). Section 5 of the IRC allows a deduction for soil and water conservation expenditures made in compliance with a conservation plan approved by the U.S. Department of Agriculture or a comparable state agency. Eligible expenses include levelling, grading, terracing, construction of diversion channels, drainage ditches, outlets and ponds, and planting windbreaks, but do not include those for pivot irrigation or the filling or draining of wetlands. These deductions are limited to 25 percent of gross farming income, and any expenses above this limit can be carried forward for use in future years, without time limit.<sup>17</sup> Further, the United States Department of Agriculture recently announced a broader Wildlife Habitat Incentives Program (WHIP) that will provide both technical assistance and cost-share payments of up to \$10,000 to landowners to help establish and improve fish and wildlife habitat under a plan and agreement.<sup>18</sup> In another example from Italy, under the *Protected Areas Act*, non-profit organizations may deduct expenses for maintaining and protecting property within a natural area designated for protection under other conservation laws.<sup>19</sup>

### **Implications**

Certain implications arise from this proposal, among them being issues related to scope, international trade, implementation and tax expenditure costs.

First, the scope of proposal number 1 could be limited by designating particular areas where it would or would not apply, although removing this disincentive may not have extensive impact on farmers, given that the most productive areas are already under cultivation and only more marginal lands would benefit. The designation of areas could encompass large areas for notification purposes, but a list of exempt properties

outside known or potential habitat of concern could be made locally available. The deduction could still be available even within habitat areas, but only where activities followed an approved plan. A new mapping project involving Environment Canada and Agriculture and Agri-Food Canada will identify where the habitat of listed species at risk and agriculture overlap, which could then be used as a basis for designating such areas.

Proposal number 2 and its alternatives also need to consider the scope of the measure; numbers 2 and 2B may include labour costs, while 2D and 2E encompass only structures and equipment and not other investments such as planting stock. Agricultural stakeholders have shown interest in general wildlife habitat measures, although these could be prioritized towards species at risk.

A second implication is that such measures would need to withstand World Trade Organization and North American Free Trade Agreement scrutiny. Further analysis than is provided in this paper would be necessary. However, given the speed with which the federal government has responded to international rulings on its taxation of split-run magazines, perhaps a similar focus and effort could be brought to bear on the development of defensible conservation deductions.

Third, such an initiative would require the landowner to prepare and have approved a simple property- or locally-specific conservation, restoration or wildlife plan. Plans, or an equivalent approach, are important to focus attention on the task at hand, and to enable monitoring of progress and prevent abuse. They help ensure a public, rather than simply a personal, benefit, and thus provide a rationale for public tax benefits. Plans could involve a range of activities, from active, profitable management (e.g. some woodlot

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<sup>17</sup> Dana Clark and David Downes, *What Price Biodiversity? Economic Incentives and Biodiversity Conservation in the United States* (Washington, D.C.: Center for International Environmental Law, 1995), p.11.

<sup>18</sup> United States Department of Agriculture, "USDA Announces New Voluntary Program to Develop Wildlife Habitat", Release No. 0325.97, Washington, 18 September 1997.

<sup>19</sup> Ian A. Bowles, Dana Clark, David Downes, and Marianne Guerin-McManus, *Encouraging Private Sector Support for Biodiversity Conservation: The Use of Economic Incentives and Legal Tools*, CI Policy Papers Volume 1/1996 (Washington, D.C.: Conservation International, 1996), p.10.

management) to a conscious and considered decision to let things be, so long as they included measures for conserving targeted species and were consistent with (but not dependent upon) any government or RENEW wildlife plans. These would be oriented towards known or potential habitat as identified by the Canadian Wildlife Service, COSEWIC, a provincial or territorial agency, a designated organization, or relevant legislation.

Plan approvals should be straightforward and not bureaucratic, and could involve federal, provincial or territorial agencies with agricultural or environmental mandates, or other private organizations or individuals, such as a Registered Professional Biologist or a RENEW recovery plan administrator. Flexibility would allow efficient, local administration with central agency backup, and conditions of delegation could ensure quality control. As with numerous programs operating now, agreements, monitoring, and periodic external reviews and reporting could ensure that multi-year plans are implemented and the program delivers public benefits. Along with information in the *Farming Income* guide and forms, a plan template and a list of standard management or restoration activities and expenses could be published and circulated, and thereby streamline and promote the program. As with the U.S. programs, commitment to providing information, expertise and other extension support would be critical; the Canadian Federation of Agriculture has suggested that the undistributed funds in the national General Adjustment Fund be used to support an integrated environmental and agricultural extension service that could assist towards this end.

Fourth, the Department of Finance may have concerns about the extent of such a tax expenditure and whether it may be best to have direct rather than indirect expenditures. The costs of the tax measure are largely offset by three factors: the cost savings of immediate restoration action rather than expensive crisis spending later; the leveraged involvement of landowners and their labour, and possibly administration by provincial agencies and private organizations; and the disallowance of clearing and levelling deductions. The above-noted mapping of endangered species on

agricultural lands may be useful in determining the extent of area that would be involved, and estimated tax costs could be derived from this data, correlated with participation rates and qualifying investments.

As with other tax proposals, the Department of Finance may question whether indirect rather than direct expenditures are the most effective and targeted measure in moving towards the intended goal. Program requirements that involve identified species and their habitats, site-oriented plans, approvals and administrative partnerships all suggest that the expenditures will be carefully and efficiently targeted for maximum benefit. Further, should federal (or other) endangered species legislation restrict landowners' activities, as was proposed and remains likely, widespread direct payments may be perceived as compensation for lost property rights or values. This would feed a U.S.-based movement that opposes all regulatory measures, and may foster misperceptions of Canadian law. By being open to voluntary subscription by landowners (subject to program conditions), indirect tax expenditures can be distanced from such sensitive issues.

## **B. Establish an Income Tax Check-off for Conservation**

### **Background**

When individual Canadian taxpayers complete their income tax forms, sometimes (although all too rarely it may seem) an individual has paid too much tax already, or the allowed credits or deductions are larger than the taxes to be paid. This produces a refund, and Revenue Canada has an obligation to send a cheque back for any amount over \$1.00. This amount may not be significant to the taxpayer and it produces an administrative headache for Revenue Canada. What if the taxpayer just told the government that all or a part of this refund could be used by the government for a particular purpose, say conservation of wildlife habitat?

This is called a tax "check-off", and it is used in many U.S. states to raise funds for worthwhile public purposes.<sup>20</sup> It has not been used in Canada to date, but

both the federal and Ontario 1996 budgets announced the intention to collect funds for the purpose of paying down the government's annual deficit and accumulated debt. The mechanics of establishing a check-off system in Canada are now being worked out and could be adapted and used for new purposes.

These funds are not government monies; they are net refunds belonging to individual taxpayers. Additional funds could be received if taxpayers were asked to indicate whether they wanted to contribute a premium above levied taxes, to be directed towards designated purposes. Such directed refunds and premiums thus could provide new monies for conservation to augment existing government budgets and private sector contributions.

A tax check-off could also be used to leverage additional resources, with the Government of Canada matching the fund in several ways. It could simply match it, dollar for dollar, or make a two-dollar contribution per donation to represent the approximate cost savings from administering and sending refunds. Alternatively, the federal government could match provincial, territorial or private organizations' supplementary contributions to the fund, thereby encouraging such involvement.

Other sources of revenue could be directed into the fund over time. As in a number of U.S. states, this could include a proportion of net Goods and Services Tax (GST) or Harmonized Sales Tax (HST) revenues from outdoor equipment sales, perhaps matched through allocations of provincial sales tax on similar items or by federal GST or HST rebates redirected by charities. Other federal rebates or payments could be specified as well, much as employers and utilities have direct deposit or withdrawal arrangements. Other possibilities include the allocation of fees, fines or restitution and restoration payments under federal wildlife legislation to such a fund, as occurs for many provincial wildlife trust funds. Authorizing legislation

should contemplate such future sources through specifically overcoming legislative barriers and enabling such additions by regulation.

Given that the core of the fund would derive from private contributions, payments from the fund would be made to programs with significant private involvement, funding, and collaboration. Again, payments would require one-to-one or higher matching ratios for projects. The fund could also be directed into provincial wildlife trust funds in the taxpayer's home province, thereby ensuring regional benefits.

The purposes for which payments would be made would depend upon the fund's characterization at the outset: is it intended and marketed for the environment or conservation in general, for species at risk, for just endangered species, or only for habitat? For two reasons, it is suggested that payments be made for habitat conservation purposes, and not simply for species at risk, or for wildlife generally. First, habitat loss is the leading cause of the decline in species, and redressing this trend will help a suite of species, not merely one or two at risk. While habitat conservation could put a priority on the habitat of species at risk (which could help market the fund), it should not be limited to this purpose. Second, there is ample authority that generates programs and funding for federal wildlife and education activities, but complementary and essential habitat issues are more complicated and sensitive because of their interaction with provincial and private property jurisdictions. As in many other areas of federal interest (e.g. health care), programs that relate to provincial jurisdiction can be achieved through providing conditional funds. This jurisdictional question is even further complicated because the fund is derived from private contributions and requires matching provincial or other funding, and is only administered in partnership with the federal government.

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20 The idea is not new in Canada. See: David J. Neave, "A Cooperative Wildlife Habitat Conservation Program", in: Canadian Wildlife Service, *A Colloquium on Wildlife Habitat Conservation in Canada* (Ottawa: Canadian Wildlife Service, 1987), pp. 111-112.

## **Proposal**

The author proposes that there be amendments to the *Income Tax Act* and its Regulations to implement the following:

1. Establish an income tax check-off program to enable taxpayers to direct certain tax refunds, rebates and premiums towards wildlife habitat conservation. New sources should be contemplated and legislative barriers removed, although further authorization would be required. Payments from the fund would require matching grants from private and other governmental sources, as well as accountability measures.

## **Examples**

As mentioned above, there are at least two examples which are under development in Canada. First, the 1996 federal budget and tax guides announced the opportunity for individuals to contribute to paying down the federal debt by sending cheques to the Receiver General to be used in the "Debt Servicing and Reduction Account".<sup>21</sup> This account was legislatively established in 1992 to fulfil and profile political promises that net GST revenues would only be applied towards reducing the deficit, and it received private contributions of \$474,000 and \$264,000 in fiscal years 1994-95 and 1995-96 respectively (apparently less in 96-97).<sup>22</sup> It could also have been established simply and administratively as a Receiver General account within Public Works and Government Services Canada.

Second, the "Ontario Opportunities Fund" was announced in the 1996 provincial budget. It involved the establishment of a separate account within the Consolidated Revenue Fund and amendments to the *Financial Administration Act*.<sup>23</sup> As noted in the Budget, the purpose of the fund is "to receive contributions from Ontarians, proceeds from major asset sales, and savings realized from the over-achievement of the Budget target" which "will be applied to reducing the debt of the Province". In its first year of operation (and for a cause that is neither charitable nor ordinarily directly supported), \$7,770.21 was received from 21 individuals.<sup>24</sup> Notice was included in the Ontario income tax forms of the opportunity to contribute to the fund by sending in a cheque to the provincial Ministry of Finance and, while there is agreement in principle, the province continues to negotiate with the federal government on how to implement a tax check-off system.<sup>25</sup>

Beyond Canada, there are also some thirty U.S. states with conservation-oriented tax check-off programs, which in 1982 raised a total of \$9 million from more than 1.8 million individuals.<sup>26</sup> These include contributions from tax refunds, and in some cases enable voluntary premiums to be added to tax payments. The revenues are modest and may initiate check-off programs for other and competing charitable purposes, but nonetheless provide for funds to leverage other contributions and also inform taxpayers through the tax guide and related publications.

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21 *General Income Tax Guide 96* (Ottawa: Revenue Canada, 1997), p.33.

22 Personal communication, Peter DeVries, Department of Finance, Fiscal Policy, 17 September 1997. The account was established by the *Debt Servicing and Reduction Account Act, 1991*, S.C. 1992, c.18, s.5. Along with GST revenues and private contributions, the account also receives proceeds of federal asset dispositions which are not otherwise committed.

23 Minister of Finance, *1996 Ontario Budget* (Toronto: Ontario Ministry of Finance, 1996), pp.5-6 and 54.

24 Personal communication, Lucie Fromstein, Ontario Ministry of Finance, 5 September 1997.

25 *Ibid*; *General Income Tax Forms 96 - Ontario* (Ottawa: Revenue Canada, 1997), p.3. Cheques are to be made payable to the "[Ontario] Minister of Finance - Ontario Opportunities Fund" and sent to Toronto, and a receipt will be issued that can be used the next year to claim a tax credit for a donation to government.

26 Calvin Sandborn, *Green Space and Growth: Conserving Natural Areas in B.C. Communities* (Victoria: British Columbia Ministry of Environment, Lands and Parks, 1996), p.129, citing a number of U.S. publications.

### **Implications**

Such a tax check-off has never been developed in Canada, and thus policy implications and administrative arrangements need to be worked out; this is still the case for the Ontario and federal funds. A number of issues can be identified in advance, however.

First, what happens if there is a tax reassessment and the refund, rebate or voluntary premium is thereby affected? Is there a presumption that increased tax liabilities can erode the refund, or that a higher refund from a lower tax levy will be directed into the fund? One possibility is for the initial or enhanced refund to be paid into the fund, regardless of reassessment; the pursuit of any higher tax liabilities should be left to future correspondence, with the taxpayer being given the opportunity to reclaim part or all of the refund. This would help retain contributions by requiring the taxpayer to direct otherwise, but may reduce initial willingness to make the contribution, given reassessment uncertainties and follow-up requirements. One possibility is a three-part check-off: one part to designate the fund of choice, a second part for the amount, and a third part for the two or three choices available in directing what should happen after a reassessment (with a default situation, as described above). The combinations of the types of contributions and the effects of reassessment would need to be examined carefully to determine the most effective, efficient and fair approach. In any case, information on the result and any follow-up options should be included in reassessment notices sent back to the taxpayer.

Second, there will undoubtedly be demands for other public interests to be included in such a check-off system; in fact, this conservation proposal is in part derived from debt reduction initiatives, although wildlife check-offs have often been the initiating model in the U.S.. There is no strong policy rationale for distinguishing between these other interests and conservation, and in approved cases such other

programs would need to be coordinated and pooled in easily administered funds. Over time, a plethora of funds may add significant administrative costs to handle fund distributions, but these can be minimized by developing standardized criteria and involving provincial and private sector participants. Nonetheless, the enhanced conservation contributions would likely exceed these costs, perhaps after an initial start-up period.

Third, given the likelihood of a proliferation of purposes, there will be concerns about how to accommodate all of these within the limited space on a tax form and in tax guides. This is relatively simple to address in the three-part check-off system suggested above. Together with a brief description of the general opportunity and the mechanics in the body of the tax guide, a supplementary page in the tax guide or forms could list all of the check-off funds and perhaps a very brief description of their purpose and past accomplishments, with each fund correlated to a number. This number, any reassessment option code (e.g. a letter), and the amount to be contributed would be entered in a specified box on a line on the tax form. This line would likely be singled out at the bottom of the form after the calculation of a tax payment or refund.

Fourth, some organizations may perceive that such federal solicitation of donations would affect their fundraising. This may be true, although such organizations and their mandates can benefit from the availability of the funds and their leveraging ability. It must be recognized that this is a unique and broad fundraising opportunity: such a solicitation is made to all Canadians, the approach "piggy-backs" on materials already produced and circulated annually, and more funds may become available from new and non-traditional sources. Nonetheless, broad sectoral discussions and support would be required to address and alleviate such concerns.

## **C. Extend Trust Tax Benefits to Stimulate Conservation Funding**

### **Background**

Additional measures may be considered in order to stimulate funding for conservation of endangered, threatened and vulnerable species and their habitat. One of these is to examine opportunities to encourage various forms of trusts to direct more of their, or their beneficiaries', dispositions towards conservation activities. There are several different kinds of trusts for income tax purposes, and they, their property and income, and their beneficiaries are taxed in varying and often complex ways. This paper cannot explore all of these aspects, but certain incentives might be entertained to encourage conservation spending by trusts.

Capital property transferred into a trust may be subject to capital gains and associated taxes in the hands of the person transferring the property. Every 21 years, the assets of a trust are deemed by law to be disposed, and immediately reacquired, and these assets must then be valued and any capital gains taxed. A disposition of an asset from the trust to a beneficiary is not taxed immediately, but will be when the beneficiary disposes of it. The income on invested capital which is retained within a "living" trust (ie. not established by a will) is taxed at the highest personal income tax level, without the availability of individual tax credits. Income or capital gain distributed to designated beneficiaries is taxed in the hands of those beneficiaries, not the trust. These are only the most simplified tax situations, and numerous other options may also be available.

### **Proposals**

The author proposes that the taxation of trusts be examined to provide incentives for contributing funds towards conservation. Such modifications may include:

1. Provide a lower tax rate or a deduction for the transfer of property into or out of a trust where some percentage (e.g. 10%) or more of the income (or capital) is distributed to a qualified conservation organization for habitat conservation purposes;
2. Increase the time period for a deemed disposition of trust capital property from 21 years to 25 years where some percentage (e.g. 10%) or more of the income is distributed to a qualified conservation organization for habitat conservation purposes in ten or more of those years; or
3. Provide that income retained within a living trust will not be taxed at the highest individual marginal tax rate, but rather the lowest rate or the normal progressive rates, where some percentage (e.g. 10%) or more of the income is distributed to a qualified conservation organization for habitat conservation purposes.

### **Implications**

The taxation of trusts is a complex subject, and any such measures will have wide impacts upon the establishment, administration and taxation of trusts and their property. Obviously, these should be fully explored before new measures are implemented.

It will be important to distinguish between trusts which are charitable foundations and thereby have a public aspect, and those which are established for private, personal motives. Existing trusts will have their constituting documents and mandates fixed, and thus their flexibility to respond to such incentives will be constrained. Where discretion is available, however, such incentives may produce investments in conservation. Trusts established after the introduction of such measures can be structured to respond more directly to the incentives.

The determination of qualified conservation organizations and conservation purposes will be an involved process. The recognition of charities by Environment Canada for ecologically sensitive land donation purposes is not sufficient in this case, since the criteria focus on those organizations which are charities, have a conservation mandate, and have the capacity to hold land. Conservation groups which are not charities and do not have the capacity to hold land may nonetheless be appropriate for administering habitat management, education or advocacy. Municipalities, provincial agencies and other

government entities, or the wildlife habitat check-off fund discussed above, may also qualify, so long as the funds are directed towards conservation purposes. A non-exhaustive "official" list of qualified organizations could be assembled by Environment Canada or by a provincial or private body for each province or territory.

Documentation of qualified transfers will be required, as will the development of appropriate forms, guides and communication of related information. As discussed above for other proposals, such measures for conservation purposes could lead to requests for parallels to support other worthwhile causes. In many cases, social programs already receive broad support, perhaps more than conservation, and therefore tax measures to stimulate such spending may be less necessary.

#### **D. Other Proposals to Encourage Land and Agreement Donations**

This section provides a number of other tax proposals for improving conservation of species at risk and other wildlife on private lands. The concepts are applicable primarily to landowners who want to donate their lands, or an agreement protecting their lands, to conservation charities. This ensures that the lands will remain under appropriate use and management. The scope of this paper does not allow extensive elaboration of these ideas, but a brief summary introduces each proposal.

##### ***Entrench i.e. Valuation Approach for Conservation Easements***

"Conservation easements" are agreements to restrict land uses that protect and remain on the land title even after the original landowner has transferred the property. The valuation and taxation of easements are complicated, and Revenue Canada considered assessing

them at nominal value.<sup>27</sup> Fortunately, in the 1997 federal budget, the Finance Minister announced that the tax treatment of donated conservation easements, and similar covenants and servitudes, would recognize their full value. However, as before, this may remain a government policy and not be entrenched in the ITA or in the Regulations. Further, easements donated to obtain a credit of up to 100 percent of income under the "ecologically sensitive land" category may not be treated in the same way as the identical easement, on the same land, donated to the same charity under the ordinary 75 percent of income rules. This does not make sense. Other comparable, long-term conservation agreements may also contain the same restrictions, have the same impact on land values, and yet would not be subject to the same valuation rules.

1. Incorporate directions to fully value long-term conservation agreements for lands either certified as ecologically sensitive or otherwise into the *Income Tax Act* and the Regulations.

##### ***Recognize One Transaction for "Bargain Sales"***

A landowner may want to donate property to a conservation organization, but also needs to realize some funds in the process. One would think that the charity could purchase the property at a discounted price, and issue a tax receipt for the difference between the fair market value and the price paid. This is the case in the United States where tax rules have been elaborated, but unfortunately Revenue Canada does not recognize such "bargain sales". Instead, Revenue Canada accepts a transaction where the conservation organization pays the full market price, and then the landowner donates some of the money back for a tax receipt.<sup>28</sup> This requires some trust, and a written agreement requiring it would invalidate it as a gift. Besides creating an additional and somewhat cumbersome procedure, the biggest problem is that it

27 For a full discussion of these issues, see: Ian C. Attridge, *Conservation Easement Valuation and Taxation in Canada*, Report No. 97-1 (Ottawa: North American Wetlands Conservation Council, 1997).

28 Keith Horner, "The Tax Treatment of Donations of Ecologically Sensitive Land" (1995 notes), as Appendix E in: Standing Senate Committee on Energy, the Environment and Natural Resources, *Protecting Places and People: Conserving Canada's Natural Heritage* (Ottawa: Senate, 1996), p.120.

requires the conservation organization to raise all of the money at the outset, rather than the often much smaller purchase price. This can prevent some large-scale donations from proceeding. Canada could look to the U.S. rules to streamline the procedure into one transaction, and thereby encourage the donation of more land into conservation ownership.

2. Recognize in one transaction the donation of property at a discounted price, called a "bargain sale".

### **Streamline Cross-Border Donations**

If an American or other non-resident owns property in Canada and wishes to donate it to a Canadian charity, but has no income from Canadian sources, the individual will have no Canadian income (or tax) against which to apply any tax receipt from the charity (this is also the case for Canadians owning land in the U.S.). In contrast, U.S. landowners can donate Canadian land to U.S. charities and get full U.S. tax deductions. The U.S. charities generally do not operate here, and often find that management of the properties is too difficult at a distance. Much of this situation is governed by the *Canada-U.S. Tax Convention*, and it also contains older and less favourable tax limits for claiming donations where U.S. residents do receive some Canadian income. Canada's *Income Tax Act* contains a number of further restrictions on cross-border donations. If such limitations were removed and the process streamlined, non-resident owners of Canadian lands (often of significant ecological value) would be more willing to donate directly to Canadian charities, and such lands would likely be more easily monitored and more effectively managed.

3. Negotiate with the United States and other countries to credit and streamline cross-border donations, and remove impediments in Canada's *Income Tax Act* and Regulations.

## **Conclusions**

These proposals are meant to share the burden with and reward farmers and woodlot owners, to generate new funding directed towards habitat conservation for species at risk, and to facilitate the donation of conservation lands and agreements. They focus on the federal *Income Tax Act* for two current reasons: first, to be considered within the 1998 budget-development process this fall, and second, to provide voluntary incentives to complement federal endangered species legislation as it is being revisited. There are examples of or similar approaches to these proposals that are working both here in Canada and elsewhere. However, these proposals are simply that, and will require further discussion, refinement and undoubtedly modification before they can be approved and implemented.

Beyond technical and policy discussions of these proposals, there must be a more fundamental commitment to develop incentives for land conservation if these or any other suggestions are to move forward. Towards this end of advocating, designing and implementing tax measures for conservation, certain elements have proven successful in the United States and would equally apply in Canada: "a persuasive vision, a recognition of urgency, compelling examples of successful partnerships, a "homegrown hero", and a broad-based, effective alliance".<sup>29</sup> With a view to success, consideration must also be given to an advocacy strategy, the structure of the initiative, and initial implementation.

Canada was recently criticized at the United Nations for its lack of progress towards biodiversity conservation measures and implementation of the *Convention on Biological Diversity* and our own *Canadian Biodiversity Strategy*. As the federal budget is balanced, the deficit is reduced, and the economy grows, there may be an enhanced opportunity to introduce economic incentive measures to foster conservation practices, especially if these measures leverage private participation and funding. Time is of

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<sup>29</sup> Phyllis Myers, "Direct Funding of Nonprofit Land Protection: A New Genre of State Land Conservation Programs", in: Eve Endicott (ed.), *Land Conservation through Public/Private Partnerships* (Covelo, California: Island Press, 1993), pp.302-313. Examples of a "homegrown hero" are presented which describe dedicated advocates and visionaries who are often current or former government employees.

the essence — economically, socially and biologically, we cannot afford a further decline in our national wildlife heritage.

These paper merely puts ideas on the table. The challenge will be to engage with such proposals, widen the circle of discussion, support technical and policy debates, and follow through with a strategy and broad base of support. The author and the Canadian Institute for Environmental Law and Policy look forward to participating in this most worthwhile endeavour.

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## Appendix 1: Summary of Recommendations

The author proposes that there be amendments to Canada's *Income Tax Act* and its Regulations to implement the following proposals.

### A. Credit Farmers and Woodlot Owners for Conservation Investments

1. Disallow costs of clearing or levelling land, unless an appropriate agency has either exempted the property or such clearing or levelling is carried out in accordance with an approved conservation or restoration plan. The application of this measure could be limited in its geographic scope by designating areas where it would (or would not) apply.
2. Enable expense deductions against current-year income of costs related to plan preparation, specific conservation or environmental mitigation equipment, and the improvement of habitat for wildlife, where there is a conservation or restoration plan approved by an appropriate federal, provincial or other agency. Ideally, these deductions would be without restriction on amount or period of carry forward, but, if necessary, the initiative could be made subject to certain caps, thresholds, documentation or non-reimbursement requirements, time limits or percentages of area or income, and could be limited to the habitat of species at risk.

Consideration may also be given to alternatives to number 2 that would somewhat modify and become integrated into existing programs, as described below.

- 2B Treat all such expenses as deductible or creditable donations to the Crown for the purposes of protecting Crown interests in wildlife.
- 2C Enable investments in equipment and land management under an approved conservation or restoration plan to qualify for full investment tax credits.

2D Create a new conservation class of depreciable property with a substantial percentage of capital cost allowance for fences, other structures, and equipment built, improved or acquired as part of an approved conservation or restoration plan.

2E Enable fences or other structures erected or improved as part of an approved conservation or restoration plan to be included as pollution reduction equipment, and thus be eligible for an accelerated rate of capital cost allowance.

### B. Establish and Income Tax Check-off for Conservation

1. Establish an income tax check-off program to enable taxpayers to direct certain tax refunds, rebates and premiums towards wildlife habitat conservation. New sources should be contemplated and legislative barriers removed, although further authorization would be required. Payments from the fund would require matching grants from private and other governmental sources, as well as accountability measures.

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3. Negotiate with the United States and other countries to credit and streamline cross-border donations, and remove impediments in Canada's *Income Tax Act* and Regulations.

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