Le Comité mixte sur la fiscalité de l'Association du Barreau canadien et l'Institut Canadien des Comptables Agréés

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Le 7 janvier 2009

L'honorable Jim Flaherty, C.P., député
Ministre des Finances
Chambre des communes
Ottawa (Ontario)

Monsieur le ministre,

Objet : Fiducies non résidentes et entités de placement étrangères

Nous vous écrivons afin de vous exhorter à accepter la recommandation du Groupe consultatif sur le régime canadien de fiscalité internationale, qui visait le réexamen des règles du projet de loi C-10 qui portaient sur les « fiducies non résidentes » (FNR) et les « entités de placement étrangères » (EPE).

Selon le Groupe consultatif, les règles proposées en matière de FNR et d'EPE devraient être examinées afin d'assurer que leur raison d'être et leur portée cadrent bien avec les recommandations faites par le Groupe consultatif dans son rapport final et avec les principes énoncés dans ce rapport qui portent sur l'imposition, au niveau international, des revenus de placements faits à l'étranger.

Dans le mémoire qu'il a adressé au Groupe consultatif, le Comité mixte du droit fiscal a formulé les recommandations suivantes au sujet des règles proposées :

> Les dispositions des règles sur les FNR devraient être remaniées de façon à ne traiter que des formes de planification fiscale à proscrire, c'est-à-dire l'utilisation de fiducies étrangères pour l'accumulation de revenus dans un paradis fiscal qui profitent aux Canadiens qui en sont les bénéficiaires ultimes.
>
> Il faudrait coordonner entre elles les règles portant sur les FNR, les EPE et le REA [revenu étranger accumulé]. Les règles sur les FNR ne devraient s'appliquer qu'aux fins d'anti-évitement mentionnées ci-dessus. Lorsqu'il y a suffisamment de renseignements disponibles

pour permettre de calculer les montants à inclure dans le revenu, les contribuables devraient avoir le droit de choisir d'assujettir aux règles du REA les entités non contrôlées (sociétés et fiducies), ainsi que les fiducies. Les règles sur les EPE devraient être remaniées de façon à ce qu'elles ne s'appliquent que dans les cas où les règles du REA ne s'appliquent pas et où il est raisonnable de croire que la génération de profits ou de revenus (qui auraient été imputables aux activités sous-jacentes de l'entité étrangère et qui auraient engendré du REA si cette entité avait été une société étrangère affiliée et contrôlée de l'investisseur canadien) était l'un des principaux motifs du placement dans l'entité étrangère. Par ailleurs, il devrait aussi y avoir une exemption de l'application des règles d'EPE lorsque le REA sous-jacent de l'entité étrangère est assujetti à des impôts étrangers élevés – c'est-à-dire à un taux d'imposition qui n'est pas beaucoup plus avantageux que les taux canadiens.

Nous sommes d'avis que nos recommandations correspondent bien aux conclusions du Groupe consultatif et, en particulier, à leurs recommandations à l'effet qu'il faudra songer à :

1. passer à un système d'exonération plus étendu en ce qui concerne l'imposition du revenu provenant de sociétés étrangères affiliées qui sont exploitées activement;
2. imposer les revenus hors exploitation de sociétés étrangères affiliées en vertu du régime de REA; et
3. élargir la définition de « société étrangère affiliée », afin qu'elle englobe des entités ou associations qui ne sont pas constituées en sociétés, telles que des fiducies.

Comme vous vous en souviendrez, des membres du Comité mixte du droit fiscal se trouvaient parmi les quatre avocats-fiscalistes et comptables qui vous ont rencontré au mois de juin afin de discuter de nos préoccupations au sujet des dispositions des règles proposées. Suite à cette réunion, le Comité mixte avait participé à des discussions supplémentaires avec des représentants de votre ministère, à qui nous avons fourni des exemples des difficultés qui sont soulevées dans la pratique par l'application de ces dispositions. Vous trouverez ci-joint, à titre informatif, une copie des notes que nous avions alors remises aux représentants de votre ministère.

Un des principes énoncés dans le rapport final du Groupe consultatif (le Rapport final) est la nécessité d'adopter des règles fiscales simples. Les règles qui sont proposées en matière de FNR et d'EPE sont cependant tout sauf simples. Dans bien des cas, il est quasiment impossible pour les contribuables de savoir si ces règles s'appliquent. Le Rapport final souligne aussi la nécessité d'adopter des « règles anti-évitement qui ciblent directement le problème, sans affecter un nombre de contribuables plus grand que ce qui est strictement nécessaire ». Les documents ci-joints donnent des exemples de la manière dont les règles qui sont proposées en matière de FNR et d'EPE affectent un éventail de contribuables beaucoup plus large qu'il ne serait nécessaire pour répondre aux préoccupations du ministère des Finances en matière de politique fiscale.

Nous vous exhortons à accepter la recommandation du Groupe consultatif visant le réexamen des règles qui sont proposées en matière de FNR et d'EPE. Le projet de loi C-10 stipulait que ces règles s'appliqueraient aux années d'imposition commençant après l'année 2006. Nous recommandons que vous reportiez la mise en application de ces règles jusqu'à ce que le processus de réexamen des règles proposées ait été complété.

Alors que la présente lettre met l'accent sur les règles en matière de FNR et d'EPE, nous aimerions aussi formuler nos observations sur deux autres questions qui ont été examinées dans le cadre du Rapport final :

1. Nous vous exhortons à accepter la recommandation du Groupe consultatif visant l'abrogation de l'article 18.2 de la *Loi de l'impôt sur le revenu*. À notre avis, l'article 18.2 ne remédie efficacement à aucun des problèmes examinés par le Groupe consultatif en matière de recours à la dette de sociétés étrangères ou de déductibilité de dépenses intérieures liées aux investissements à l'étranger. En outre, cette disposition nuit à la compétitivité, l'efficacité et l'impartialité du régime canadien de fiscalité internationale. Dans la conjoncture actuelle, il est essentiel de veiller à ce que le régime fiscal canadien favorise la compétitivité des entreprises canadiennes (plutôt que d'y nuire).

   La mise en application de l'article 18.2 est reportée aux périodes d'imposition commençant après l'année 2011, afin de donner aux contribuables le temps de réorganiser leurs activités de manière à éviter les effets de cet article. Nous vous recommandons d'annoncer dans les meilleurs délais votre intention d'abroger l'article 18.2, afin d'éviter des pertes de temps et des dépenses inutiles aux contribuables affectés qui réorganiseront leurs activités dans le but de se plier aux exigences de cette disposition.

2. Le Groupe consultatif a recommandé l'adoption d'une mesure visant à enrayer les transactions d'abandon de dettes qui sont effectuées pour des raisons fiscales par des sociétés apparentées. Bien que nous comprenions les raisons politiques d'une telle mesure, il est à notre avis important de veiller à ce que toute législation de mise en œuvre soit rédigée conformément aux principes énoncés par le Groupe consultatif, c'est-à-dire qu'un règlement fiscal devrait être simple et cibler spécifiquement le problème visé sans outrepasser ses objectifs précis. Nous sommes aussi d'avis qu'il est important de prévoir une généreuse clause de droits acquis en matière d'exonération de dette (et de tout refinancement de cette dette) dans la mesure où la dette existait ou était reconnue avant que de nouvelles règles n'aient été annoncées.

Pour terminer, nous sommes d'accord avec le Groupe consultatif que toute proposition devrait faire l'objet d'un processus de consultation approfondie auprès de personnes concernées, avant que des avant-projets de loi ou de règlement ne soient rendus publics. Le Comité mixte du droit fiscal serait très heureux de participer à ce processus.

Nous vous prions d'agréer, monsieur le ministre, l'expression de nos sentiments distingués.

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Président, Comité de l'impôt sur le revenu
L'Institut canadien des comptables agréés

Paul Tamaki
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cc. Brian Ernewein, directeur général, Direction de la politique de l'impôt, ministère des Finances Canada
Gérard Lalonde, directeur, Division de la législation de l'impôt, Direction de la politique de l'impôt, ministère des Finances Canada

November 19, 2008

CBA – CICA Joint Committee on Taxation

Non-Resident Trust (NRT) and Foreign Investment Entity (NRT) Provisions

Points to Discuss

The Joint Committee's views and recommendations on the proposed NRT and FIE provisions are set out in our July 15, 2008 submission to the Advisory Panel on Canada's System of International Taxation.

The following are examples of concerns that arise in practice under the existing proposals.[1] These comments are not intended to be exhaustive.

A. Non Resident Trusts (NRT)

1. Paragraph 94(2)(c) is unnecessarily broad and catches arrangements where there is no anti-avoidance motive.

Example

A foreign trust with no Canadian contributor or Canadian beneficiary acquires a portfolio investment in publicly-listed shares of Can Pubco, a widely held Canadian public company. Can Pubco transfers an asset to a subsidiary of Can Pubco, for an interest-free promissory note. This transfer would not have occurred on the same terms if the transferor and the transferee dealt with each other at arm's length.

The transaction would not satisfy the requirements of being an "arm's length transfer" as defined in subsection 94(1). Paragraph 94(2)(c) would deem Can Pubco to have transferred property to the foreign trust, resulting in potential Canadian tax liability for both Can Pubco, the foreign trust and its beneficiaries. This would also appear to be the case even where the transaction was completed before the foreign trust owned any shares of Can Pubco.

There would be the same result if the transfer is from one controlled foreign affiliate of Can Pubco to a second entity in which Can Pubco has a direct or indirect interest. Under paragraph 94(2)(l), Can Pubco would be deemed to have jointly made the transfer to the second entity if the transfer is made at the direction of or with the acquiescence of Can Pubco. If Can Pubco controls the transferor, it may be difficult to conclude that Can Pubco did not acquiesce in the transfer.

There also would be the same result in the case of an intercompany loan (paragraph 94(2)(c)), guarantee (paragraph 94(2)(e)) or provision of services (paragraph 94(2)(f)) by Can Pubco (or any Canadian subsidiary or controlled foreign affiliate of Can Pubco) in favour of any other entity in which Can Pubco has a direct or indirect interest, if the terms are not arm's -length.

2. Paragraph 94(2)(f) applies with respect to services rendered directly or indirectly to a trust. In order for a service to a trust to not be deemed to be a transfer to the trust

[1] References to provisions of the Income Tax Act (the "Act") are to the provisions of the Act as proposed to be amended by Bill C-10.

under the NRT rules, the service must be an exempt service or an arm's length transfer. To be an exempt service or arm's length transfer, it must be reasonable to conclude, having regard *only* to the service provided to the trust, that the provider would have been willing to provide the service if the provider had been dealing at arm's length with the trust, and the terms, conditions and circumstances under which the service was provided would have been acceptable to the service provider if the service provider dealt at arm's length with the trust.

Legitimate arrangements may not on arm's length terms, especially if analysed on an unbundled basis.

Example

A Canadian resident individual with a particular skill or knowledge (such as a lawyer, accountant or investment advisor) provides assistance (other than with respect to trust administration) to a foreign trust simply because of a personal relationship with the beneficiaries or trustees of the trust or for any other non-tax reason. The individual does not charge for the services or charges less than an arm's-length amount.

Paragraph 94(2)(f) would cause the Canadian to have made a contribution to the trust and cause the trust to be deemed resident in Canada.

There would be the same result if the services are provided to a corporation in which the trust had an interest because paragraphs 94(2)(f) and 94(2)(c) would deem the individual to have transferred property to the trust.

Example

An individual resident in Canada is both a 50% shareholder and director of NRCo, a non-resident private company. The other 50% of the shares of NRCo are held by a foreign trust with unrelated foreign beneficiaries and the settlor of the foreign trust is the other director of NRCo. The two directors act without compensation.

Since both the exempt service and arm's length transfer definitions require that *only* the service and the compensation for the service be considered, the Canadian director would be deemed under paragraph 94(2)(f) to have made a transfer of property to the trust and the trust would be deemed to be resident in Canada thereby creating potential Canadian tax liability for the Canadian director, the trust and its beneficiaries.

3. In determining whether the rules apply, it is irrelevant whether the trust or its beneficiaries are taxable in their own jurisdictions at rates of tax comparable to the Canadian rates. Many Canadians create trusts in other jurisdictions for legitimate family reasons unrelated to tax.

Example

Canadian parents settle a trust for a child who lives outside Canada. For legal and family (non-tax) reasons, they wish to have a relative or family friend in that jurisdiction to act as trustee.

Where it can clearly be demonstrated that there is no tax avoidance motive or possibility of tax avoidance, a foreign trust should not be subject to the NRT rules. This can reasonably be expected to be the case, for example, where all of the income of the trust is taxed in either the trust or a beneficiary at rates comparable to Canadian rates. At the very least, it should be possible to resolve the matter of residence using the competent authority procedures of any applicable tax convention.

4. Foreign tax credits do not deal satisfactorily with double taxation issues, particularly for those trusts that are actually resident in a country that has a sophisticated tax system and a tax rate that is comparable to the Canadian tax rate.

If the trust has Canadian source income then no foreign tax credit can be claimed for Canadian tax purposes for any non-Canadian tax paid on that income. Subsection 20(11) can also limit the amount of the foreign tax credit claim to 15% of any non-Canadian source interest, dividend or similar property income.

The timing of deductions and income inclusions in the country of actual residence may differ from the year in which deductions or income is included for Canadian tax purposes.

For investment income (dividends, interest etc) there is no ability for Canadian tax purposes to carry foreign taxes paid in one year to another year.

The Canadian tax payable by the trust is determined using Canadian dollar values whereas the trust's foreign tax is determined using the relevant foreign currency. Thus the trust's capital gain for foreign tax purposes may be different from the gain as determined for Canadian tax purposes.

The basis for recognizing income in the foreign jurisdiction may be different from the Canadian rules.

Example

A US trust holds shares of a corporation and receives dividends from the corporation.

The US taxation of the dividend depends on whether the corporation is a fiscally transparent entity for US tax purposes, and if it is not fiscally transparent, whether the corporation is considered to have sufficient earning and profits for US tax purposes. These concepts are not applicable for Canadian tax purposes.

The application of the "21 year rule" under subsection 104(4) can also result in Canadian tax liability where there is no liability in the US. '

Double taxation relief may be available under a tax treaty, but this is a very inefficient process if it is necessary for a deemed resident trust to continuously approach the Canadian competent authority (or the competent authority of the country of actual residence) to eliminate double taxation problems.

5. Foreign tax credits may not be sufficient to deal with double taxation issues under the NRT provisions.

   Example

   A US trust is deemed resident in Canada because there is a Canadian resident contributor. Trust income is distributed by the trust to the US beneficiaries and is subject to Canadian withholding tax by virtue of subparagraph 94(3)(a)(ix). From a US perspective that Canadian withholding tax is on US source income and as a result a US foreign tax credit may not be allowed.

   A foreign tax credit would not relieve the trust and the Canadian contributor from liability in respect of Part XIII withholding tax on the distribution.

6. Paragraph 94(2)(n) and the definition of "non-resident time" can provide anomalous results.

   Example

   NRT, a non resident trust with Canadian beneficiaries, was settled by Mr. X, a non-resident individual, and is not subject to section 94 because Mr. X was not a connected contributor to the trust. Mr. X dies and NRT transfers its assets to NRT II, another non-resident trust with Canadian beneficiaries.

   NRT II will be subject to section 94 because paragraph 94(2)(n) deems a contribution to NRT to be a contributed to NRT II *at the time of the subsequent transfer*. Thus Mr. X is deemed to have made a transfer to the NRT II at the time of the subsequent transfer, but as he is dead at that time the time of contribution cannot be at a "non-resident time" because the definition of non-resident time ends at the time of death. Therefore, Mr. X is deemed to have made a transfer at a time other than a non-resident time and thereby becomes a connected contributed to NRT II and NRT II is subject to section 94.

7. The definition of "successor beneficiary" in subsection 94(1) is too narrow. It is not uncommon for nieces and nephews to be included as beneficiaries of an estate or trust particularly if all of the settlor's or testator's children are deceased at the time of a distribution.

   It is also not clear from the definition of successor beneficiary that a person would be a successor beneficiary if their entitlement to trust income or capital arises after the death of more than one person.

8. Under the NRT rules, Canadian taxpayers may unknowingly be contributors to a foreign trust and thereby be jointly and severally liable for all of the taxes of the trust.

The limitation in subsection 94(7) may not apply if the Canadian contributor does not file form T1141 on a timely basis. In many cases it is not reasonable to expect that the foreign trust will pay the Canadian tax or that the Canadian contributor can compel payment. Under the "revenue rule," one sovereign state will not enforce the tax laws of another. Furthermore, foreign trustees may be unwilling or unable to provide the Canadian contributor with information to contest a Canadian assessment.

9. The exemption in paragraph (h) of the definition of "exempt foreign trust" in subsection 94(1) is intended to cover investments in genuine commercial trusts, but in practice it is largely unworkable and ineffective because it does not reflect the reality of how investors invest in commercial trusts, or the structure and features of such trusts. In practice, investors and non-resident trusts have found it impossible to obtain the information that is required to determine whether the requirements of the exemption are satisfied. Given the significant liability that may be imposed on a commercial trust and its unitholders, managers of such funds may not permit Canadians to invest if there is any uncertainty whether the NRT rules may apply.

These concerns apply to both taxable and non-taxable investors. The legislative changes described in the April 2008 comfort letters issued by the Department of Finance will provide only limited assistance in excluding legitimate commercial trusts from the application of the NRT rules for a limited group of investors.

Example

Many investment funds are structured as "funds of funds" being an investment fund that itself invests in a wide array of other investment funds some of which may be non-resident trusts or may be corporations or partnerships that, in turn, invest in non-resident trusts. An investor in the top fund may have no idea whether or when that top fund will hold a direct or indirect investment in a non-resident trust. The manager of the top fund may have limited influence over a non-resident trust in which the top fund directly or indirectly invests. Consequently, it may be impossible to determine, for example, whether any Canadian contributor holds more than 10% of any class of the non-resident trust's units, or whether the non-resident trust holds restricted property.

A fund may be a trust, partnership or corporation. A Canadian investor can be caught by the NRT provisions even on an investment in a corporation, if that corporation makes a transfer to a non-exempt foreign trust which is caught by paragraph (b) or (c) of the definition of "contribution."

Example

A foreign corporation issues shares to the public and uses the funds to acquire units in non-resident trust. A Canadian individual subscribes for shares of the foreign corporation under the offering. As a result, there is a series of transactions whereby the individual transfers property to the foreign corporation and there is another transfer of property to the non-resident trust, and the second transfer is in respect of the first transfer.

> The Canadian individual is a “contributor” to the underlying non-resident trust under paragraph (b) of the definition of “contributor” in subsection 94(1). The exemption in that definition in respect of arm’s length transfers is not available if one of the reasons for both transfers is the acquisition by any entity (i.e., the top foreign corporation) of an interest as beneficiary under the non-resident trust (see paragraph (a) of the definition of “arm’s length transfer”). As a result, the non-resident trust is deemed to be resident in Canada.

The exception for commercial trusts in paragraph (h) of the definition of exempt foreign trust applies only were units in the trust are “specified fixed interests.” Paragraph (c) of the definition of “specified fixed interest” provides that the only manner in which any part of an interest in a commercial trust may cease is by way of a “transfer” that is a “disposition.” Commercial trusts may undergo transactions which do not involve a redemption or other form of transfer of units.

> Example
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> A commercial trust undergoes a merger whereby units of a commercial trust cease to exist and unitholders receive units of a new trust or other securities, without a specific redemption of their units.
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> Because the definition of “specified fixed interest” provides that the only way that an interest in the trust *may* cease is by way of a transfer, the mere possibility that units may cease to exist under such a transaction (i.e., without a transfer) may be sufficient to disqualify the trust from the outset.

Paragraph (d) of the definition of “specified fixed interest” provides that no amount of the income or capital of the trust that any entity may receive at any time can depend on the exercise of a “discretionary power.” Commercial trust declarations are not drafted with Canadian tax laws in mind and can provide trustees with discretion in respect of a number of matters which could affect the amount or timing or income or capital distributions of the trust. The technical notes indicate that the provision means in very general terms that no entity may hold a power to appoint beneficiaries under the trust, but the legislation itself is clearly much broader and there is significant uncertainty regarding how the courts or the CRA would interpret such language. It may also be impossible for some investors in non-resident trusts to obtain the relevant trust deeds in order to even identify the existence or nature of any discretionary power that might influence the particular amount of income or capital distributed by the trust.

> Example
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> The declaration of trust for a commercial trust provides for multiple classes of units with different distribution entitlements. The declaration of trust provides that the trustees shall make regular distributions of “distributable cash” on a class by class basis, determined by deducting such reserves or other amounts as the trustees may determine, and may pay special distributions in such amounts and at such times as the trustees may determine in their sole discretion. The amount of distributable cash received by the trust

also depends on the exercise of discretion by underlying entities of the trust.

Since the trust has multiple classes of units, distributions are not made pro rata to all unitholders of all classes. Thus it is not clear whether CRA administrative practice with respect to the existing provisions applies: see for example CRA document 903515 (January 15, 1991).

Clause (d)(ii)(C) of the definition of "specified contributor" effectively requires units of a commercial trust to be acquired at fair market value whereas many foreign funds provide flexibility for other arrangements.

Example

A commercial trusts permits distributions to be reinvested at net asset value, which may not be fair market value. The trust also permits additional investments through rights offerings made available to all unitholders.

If a commercial trust cannot qualify under the exemption in respect of commercial funds with more than 150 qualifying investors, it must meet the more restrictive test in clause (h)(ii)(B) under which the trust cannot hold any "restricted property." We understand that the provision is intended to cover participating shares of a corporation acquired by the trust as part of an international estate freeze, but the wording is much broader than this.

Example

A foreign commercial trust issues units to the public and uses the funds to acquire redeemable shares of a wholly owned corporate subsidiary of the foreign trust.

The redeemable shares are restricted property because they are specified shares of a closely held corporation acquired by any entity in exchange for any property.

The exemption in clause (h)(ii)(B) also requires a form to be completed and filed with Canada Revenue Agency by or on behalf of the fund. In many cases, it is unreasonable to expect that a fund will file this form or authorize it to be filed on its behalf.

Even where a Canadian taxpayer invests in an exempt foreign trust (and might therefore think that the NRT rules cannot possibly apply), the rules might nevertheless apply as a result of the application of paragraph 95(2)(n), which provides that a contribution made by a particular trust to another trust is deemed to have been made jointly by the particular trust and by each entity that is a contributor to the particular trust. There is a similar concern discussed above under the broad definition of "contribution" in subsection 94(1).

Example

An exempt foreign trust issues units to the public and uses the funds to acquire units of a second non-resident trust.

Canadian unitholders of the exempt foreign trust are deemed to have made a contribution to the second non-resident trust. If the second non-resident trust is not an exempt foreign trust, the NRT provisions apply to the second non-resident trust and to the resident contributors to the exempt foreign trust.

10. Paragraph (f) of the definition of exempt foreign trust does not permit Canadian employees of foreign multinationals to participate in employee share plans even where they make up a very small proportion of the total plan membership.

B. Foreign Investment Entities

1. The major concern with the FIE rules is that it is not practical to expect that investors will be able to make the factual determinations necessary to decide whether the FIE rules apply to an investment or, if the investment is a FIE, to determine the amount of income from the investment which must be reported.

Example

A Canadian has a minority interest in a foreign trust that is not an exempt foreign trust under the NRT rules but is an FIE.

For the purpose of applying the FIE rules to the investment, the Canadian investor's designated cost of the investment is determined under paragraph 94.1(2)(c) based upon the underlying assets of the trust and this determination must be made on a month-by-month basis. This requires information from the trust that may not be available to the beneficiary.

Example

A Canadian has a portfolio investment in shares of a Luxembourg company whose shares are listed on the Luxembourg stock exchange.

The investment would not be an exempt interest unless the Luxembourg company is resident in a country in which there is a designated stock exchange. The Canadian investor would be unlikely to be able to confirm the residence of the company under the common law test of mind and management as this would require information as to the authority of the board of directors and the place where they exercise central management and control.

2. A "specified interest" is any interest of a beneficiary under a trust (other than trust referred to in paragraph (h) of the definition of "exempt foreign trust" in subsection 94(1)), excluding a beneficial interest under which every amount of the income and capital of the trust that the individual may receive depends on the exercise of a discretionary power. This is unnecessarily broad.

Example

A Canadian resident individual is one of a number of residual beneficiaries of a foreign trust. The trustees have discretion to make distributions of income or capital to certain beneficiaries during the term of the trust. According to the terms of the trust, any remaining amount in the estate is to be distributed pro rata to residual beneficiaries on termination of the trust.

Since the Canadian resident's entitlement does not depend on the exercise of a discretionary power, the interest is caught by the FIE provisions. This may be the case even though the Canadian beneficiary may not have been advised of his or her interest in the estate.

3. The tracking interests portion of the FIE rules is difficult to interpret and apply.

Example

A Canadian taxpayer acquires 100% of the outstanding common shares of USco., a United States corporation. USco owns 40% of the outstanding common shares of USco2, and 40% of the outstanding common shares of USco3. USco2 and USco3 each carry on an active business in the United States.

In testing whether the tracking interest rule applies to the shares of USco it is necessary to first determine what are the relevant "tracked properties" in paragraph 94.2(9)(d). Here, it is unclear whether the tracked properties are the shares of USco2, the assets of USco2, the shares of USco3, the assets of USco3, or some combination thereof. It is then necessary to determine whether the "tracked properties" are owned by USco to determine whether it is a "tracking entity" as defined in subsection 94.2(1), which requires the tracked properties to be identified. If the tracked properties are all owned by USco then it is necessary to determine whether the fair market value of those properties is more than 90% of the fair market value of all USco's property, or whether the fair market value of any tracked property that is "investment property" exceeds 50% of the tracked property. Even if it were possible to identify the tracked properties, the relevant fair market values may not be available. If any tracked property is not owned by USco then it is necessary to determine whether USco (or any non-arm's length entity) owns investment property (or substituted property) that may be used to satisfy right to income from the tracked property referred to in paragraph 94.2(9)(d).

4. The definition of "exempt business" should not exclude a business that is carried on by an exempt foreign trust.

Example

A Canadian resident acquires units of a non-resident trust, the units of which are listed and actively traded on a designated stock exchange. The principal purpose of the trust is to derive income from the rental of real estate and, except for the carve out for exempt foreign trusts in the preamble of the exempt business definition, the trust would carry on an exempt business.

The sole fact that the trust is an exempt foreign trust should not preclude it from carrying on an exempt business under the FIE rules.