



THE INVESTMENT FUNDS INSTITUTE OF CANADA  
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

**BY EMAIL**

March 7, 2011

Mr. Gérard Lalonde  
Director, Tax Legislation Division  
Finance Canada  
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Ottawa, ON K1A 0G5  
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Dear Mr. Lalonde:

**Re: Designation of Foreign Income and Tax by a Trust**

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I am writing as a follow-up to the meeting held on June 2, 2010 to request a technical amendment to subsections 104(22) and (22.1) of the *Income Tax Act* (Canada) (ITA) to permit a beneficiary of a trust who has received foreign source income from the trust to choose whether to claim a foreign tax credit under section 126 of the ITA or a deduction under subsections 20(11) or (12) of the ITA for foreign taxes paid by the trust.

Currently, the designation of foreign source income and foreign taxes by a trust under subsections 104(22) and (22.1) only applies for the purposes of claiming a foreign tax credit under section 126, but not for the purposes of claiming a foreign tax deduction under subsections 20(11) or (12). There does not appear to be a policy reason for this distinction.

This issue has become increasingly relevant to the mutual fund industry because of the use of fund-on-fund structures – *i.e.*, where one mutual fund trust invests in another mutual fund trust. Each year, mutual fund trusts distribute a sufficient amount of their income and claim a deduction under subsection 104(6) so that the trust is not subject to tax under Part I of the ITA. Mutual fund trusts designate their distributed capital gains under subsection 104(21) and Canadian dividends under subsection 104(19) so that the character of those types of income flows through to the beneficiaries of the trust. However, frequently, a mutual fund trust will choose to deduct the foreign taxes paid by it from its foreign source income when calculating its income under the ITA, rather than distributing the foreign source income to beneficiaries and designating amounts under subsections 104(22) and (22.1), especially when the amount of the foreign tax that would be designated per beneficiary is nominal or negligible. However, this choice is not available to a trust that receives foreign source income (and related foreign taxes) from an underlying trust fund.



Mr. Gérard Lalonde

Re: IFIC Request for Technical Amendment to Subsection 104(22) and (22.1)

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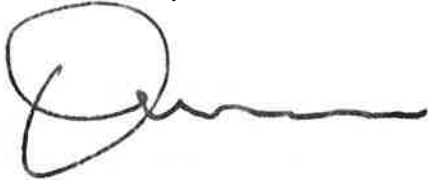
To address this issue, we request that subsections 104(22) and (22.1) be amended as follows:

**104(22) Designation of foreign source income by a trust** -- For the purposes of subsections 20(11) and (12), this subsection, subsection (22.1) and section 126, such portion of a trust's income...

**104(22.1) Foreign tax deemed paid by beneficiary** – Where a taxpayer is a beneficiary under a trust, for the purposes of subsections 20(11) and (12), this subsection and section 126, the taxpayer shall be deemed ....

I would be pleased to discuss this with you at your convenience.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'Jon Cockerline', with a large loop at the start and a long horizontal stroke extending to the right.

Jon Cockerline

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