



November 16, 2007

Reference number: IFA 2007-0003

XXX

Dear XXX:

Re: XXX

Thank you for your letter dated XXX, requesting a technical interpretation on behalf of XXX, with respect to the provisions of the *International Financial Activity Act* ("IFA Act"). The issues outlined in your letter were further expanded and discussed in our telephone conversation with XXX on XXX. We understand that you held further discussions with the Ministry of Finance who provided a verbal response XXX. I regret the delay in responding.

Your interpretations requested relate to XXX's financial activities performed at its corporate head office in Vancouver, British Columbia.

An "international financial business" (IFB) is defined under section 1 of the IFA Act as a business carried on by a corporation through a fixed place of business in British Columbia as part of an active business of the corporation, if all the activities of the business are "international financial activities". For these purposes, active business has the same meaning as under section 248(1) of the *Income Tax Act* (Canada) (federal Act) and "international financial activities" has the meaning as provided in section 2 of the IFA Act.

Section 2 of the IFA Act lists the activities related to deposits and loans that qualify as international financial activities including:

- section 2(2)(a) accepting deposits in any currency from a non-resident person, or in respect of a prescribed business from a person carrying on the business;
- section 2(2)(b) making deposits in any currency with a non-resident person, or in respect of a prescribed business with a person carrying on the business;

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- section 2(2)(c) making loans in any currency to a non-resident person or in respect of a prescribed business to a person carrying on the business, and
- section 2(2)(d) borrowing in any currency from a non-resident person or in respect of a prescribed business to a person carrying on the business.

Corporations may routinely buy and/or sell debt securities such as treasury bills, banker's acceptances, bonds and commercial paper with non-residents as part of their normal treasury function operations. These debt securities are normally quoted in an active market. What represents securities for the purpose of the IFA Act is guided by the definitions provided in the *Interpretation Act* (British Columbia) and the *Securities Act* (British Columbia).

It is our view that these types of securities are obligations, but obligations that are not loans for the purposes of the IFA Act. An exception to this interpretation is where the IFA registrant is the first borrower/lender.

Where an IFA registrant is the first borrower/lender of a debt security and that security is held to maturity (or disposed of prior to maturity), the income earned will qualify for inclusion as IFB income. For registered corporations that are not securities corporations, any other transactions involving debt securities bought and sold on a secondary market will result in no portion of any income (loss) related to that security qualifying for inclusion as IFB income.

We understand that you have discussed this issue with the Ministry of Finance.

Those activities related to dealing in securities by such registered corporations that are not securities corporations that will qualify as international financial activities under sections 2(2)(g)(ii) or (iii) include:

- dealing in securities (including derivatives) as principal for the purposes of managing the financial risk of a non-resident person, other than the risk with respect to the change in value of a commodity (section 2(2)(g)(ii)). While this would include certain hedging transactions, income derived from speculative trading or from the sale of commodities would not qualify, and
- dealing in securities (including derivatives) as agent for a non-resident of Canada (section 2(2)(g)(iii)).

Activities involving dealing in securities of the capital stock of the corporation or its affiliates are excluded from qualifying as international financial activities.

Investment management activities that qualify as international financial activities under the IFA Act may also include:

- section 2(2)(k), managing for a non-resident, for a fee or commission, foreign exchange activities for non-resident persons;
- section 2(2)(l), managing investments for non-resident persons, and
- section 2(2)(m) managing for a fee or commission and for residents investments in securities issued by a non-resident that are not listed on a Canadian stock exchange.

Section 19(1) of the IFA Act defines IFB income as the income or loss, as determined under Subdivision b of Division B of Part I of the federal Act, of the international financial business as if the business's income for the taxation year was only from international financial activities other than patent activities for that part of the taxation year that the corporation was a registered corporation. Any allocation method chosen to comply with the IFA Act should be reasonable in the circumstances and should substantiate the amount claimed.

The income or loss from currency hedging, where the hedge is incident to an international financial activity and is not of a speculative nature, and where the registrant is not a securities corporation, may be included for the purposes of determining IFB income where there is:

- a high degree of correlation between the hedging transaction and the international financial activity;
- formal documentation related to the hedging activity, and
- periodic assessment of the effectiveness of the hedging relationship.

We trust that the above comments are of assistance. This letter is not a ruling and consequently is not binding on the Ministry of Small Business and Revenue.

Yours truly,

Jeffrey S. Krasnick, CA
Director
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