



May 4, 2010

Reference number: IFA 2010-0001

XXX

Dear XXX:

Re: XXX

Thank you for your letter dated XXX, requesting a technical interpretation with respect to the provisions of the *International Financial Activity Act* ("IFA Act") in relation to certain proposed activities of XXX. The issues outlined in your letter were further discussed in a phone conversation on XXX and follow-up email of XXX from XXX.

FACTS

Our understanding of the facts is as follows:

1. XXX;
2. XXX US operations are managed by XXX, an indirectly owned subsidiary of XXX. XXX collection department is currently supported by over XXX US debt collectors located in various branches over the United States;
3. XXX's customers are primarily located in the United States, although some revenues may be derived from customers outside of North America;
4. XXX incorporated a fully owned subsidiary, XXX, on XXX under the *Canada Business Corporations Act*, and
5. XXX is registered with the province under the IFA Act.

Our understanding of the proposed transactions is as follows:

1. XXX proposes to transfer the accounts receivable and collection management function for the North America region from XXX to a dedicated factoring service centre in XXX, BC under XXX.

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2. The proposed factoring arrangement will be implemented in a phased approach, with the aim of including all US regions within approximately XXX from the expected start date.
3. XXX will on an ongoing basis purchase US trade receivables due from XXX.
4. XXX will be under no obligation to purchase any of the accounts receivable offered by XXX. Any US trade receivables purchased will be on a non-recourse and arm's length basis.
5. XXX will undertake the collection process for the receivables purchased and will receive payment for the receivables directly from the customer.
6. XXX will initially hire XXX who will carry on the factoring activity from XXX's XXX office. XXX.
7. XXX will be fully responsible for collecting the accepted receivables including filing XXX and legal actions where necessary.
8. XXX.
9. XXX will enter into a service agreement with an affiliated corporation, XXX, for payroll, human resource and information technologies support services. XXX will pay XXX prevailing market rates for these services.
10. XXX will operate solely from a permanent establishment in XXX and XXX will have no permanent establishments outside of British Columbia.
11. XXX will make an election to report in a functional currency (US\$) for Canadian federal and provincial income tax purposes.

ACT¹ AND REGULATION

An "international financial business" (IFB) is defined under section 1 of the IFA Act as follows:

- "international financial business", in relation to a corporation, means a business
- (a) that is a qualifying business carried on by the corporation through a fixed place of business in British Columbia, and
 - (b) all the activities of which are international financial activities;

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¹ This technical interpretation does not reflect any proposed changes to the *International Financial Activity Act* by Bill 19, *Finance Statutes Amendment Act (No. 2)*, 2010, introduced April 29, 2010.

To be a “qualifying business”, a corporation will have to satisfy one of the following criteria establishing a substantial British Columbia presence:

- the corporation carries on an active business²;
- the corporation carries on a separate business within a corporation that carries on an active business where that separate business earns income principally from property (such as treasury activities), other than from property used in or incident to the active business, or
- the corporation is affiliated with another corporation that carries on an active business, the corporation pays at least \$300,000 in annual salary and wages to employees employed in the active conduct of the corporation’s qualifying business and the corporation has “capital employed in BC”³ of at least \$10 million.

The IFA Act defines “business” as having the same meaning as under section 248(1) of the *Income Tax Act* (Canada) (federal Act), except it does not include an adventure or concern in the nature of trade. To qualify as an international financial business, “all the activities” of the “business” must be “international financial activities”. For this purpose, “international financial activities” has the meaning as provided in section 2 of the IFA Act.

INTERPRETATION

The letter requests our interpretation as to whether:

- XXX will qualify as carrying on an international financial business as defined under section 1 of the IFA Act;
- the factoring activity as described in the proposed transactions section above will be regarded as an international financial activity as defined in subsection 2(2) of Part 1 of the IFA Act;
- XXX will be regarded as having met the requirements to apply to register with the Commissioner, as set out in section 9 of Part 2 of the IFA Act;
- XXX’s income derived from the proposed factoring activity will be treated as IFB income as defined in subsection 19(1) of the IFA Act, and
- XXX’s IFB income, denominated and computed in its US dollar functional currency will be respected for the purposes of the IFA Act.

We note that XXX has already been registered under the IFA Act. Accordingly, we will not provide any further comments on that issue.

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² For this purpose, active business has the same meaning as under section 248(1) of the *Income Tax Act* (Canada) (federal Act).

³ Defined to mean an amount equal to the total capital stock of the corporation multiplied by the corporation’s BC taxable income for the year divided by the Corporations federal taxable income for the year.

Section 2 of the IFA Act lists the activities that qualify as international financial activities for the purposes of the Act, including, in section 2(2)(o), collecting trade accounts that are receivable from a non-resident person and have been bought outright from the seller and without recourse to the seller (commonly known as factoring).

For the purposes of the federal Act, the Canada Revenue Agency has interpreted “active income” to include income from a non-arm’s length factoring arrangement on terms comparable to those between arm’s length parties, carried out on a regular and ongoing basis. We agree with this interpretation for purposes of applying the IFA Act.

For the purposes of section 2(2)(o) of the IFA Act, trade accounts receivable may be purchased from a resident or non-resident, on an arm’s length or non-arm’s length basis, so long as the contractual obligation to pay the debts which have been purchased rests with the non-resident person.

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.

Section 20 provides that in determining IFB income, transactions between related parties and affiliated corporations must be valued at fair market value. If the transaction is not at fair market value, the Commissioner may set the transaction price to reflect fair market value.

The IFA Act does not contain provisions relating to the functional currency reporting election permitted by section 261 of the federal Act. Our interpretations can only relate to specific provisions in the IFA Act. We can, however, offer the following general comment in relation to your request concerning functional currency. Where a corporation has filed an income tax return for a functional currency year under section 261 of the federal Act, the province will accept a return prepared in the elected functional currency for that year as filed in accordance with section 24 of the IFA Act.

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

Yours truly,

Marcia Knowles, CA
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Income Taxation Branch