

Document number:2000-0018195
Income Tax Act:248(1), 6(1)(g)

Please note that the following document, although believed to be correct at the time of issue, may not represent the current position of the Department.

PRINCIPAL ISSUES:

1. Are contributions to a U.S. 403(b) plan deductible for Canadian income tax purposes. 2. If not, is there double taxation if the contributions and accumulated income are used to purchase a deferred annuity upon the retirement of the contributor?

POSITION:

1. No.

2. No.

REASONS:

1. There is no deduction under the Income Tax Act("Act") for contributions by an employee to a non-resident pension plan (Note: This plan is not a 207.6(5) arrangement). 2. The plan is an employee benefit plan for Canadian tax purposes. Income therefrom excludes employee contributions (6(1)(g)(ii)).

2000-001819
G. Kauppinen

August 10, 2000

Dear XXXXXXXXXXXX :

Re: Contributions to U.S. 403(b) Pension Plans

This is in reply to your letter dated March 27, 2000 on the above-noted subject.

You have advised us of the following:

1. You are a citizen and resident of Canada.
2. You are employed by XXXXXXXXXXXX .
3. Your employer's employee pension plan has a mandatory "defined contribution" which is withheld from your salary at source. These "defined contributions" are "tax deferred" for U.S. purposes pursuant to paragraph 403(b) of the U.S. Internal Revenue Code (the "Code") (i.e. they are not included in your gross (form W-2) income for U.S. income tax purposes).
4. You can also elect under subsection 403(b) of the Code to contribute additional voluntary amounts to the pension plan which are also "tax-deferred" for U.S. income tax purposes. All of your contributions and accumulated income thereon will be converted into an annuity for you when you retire.
5. During our telephone conversation on or about June 28, 2000 (XXXXXXXXXXXX you advised us that, in addition to your contributions to the plan, your employer also makes contributions for you (which are not part of your salary).

We assume that the pension plan is not subject to U.S. tax on its accumulating income.

You have asked whether your contributions to the pension plan must be added back in computing your income for Canadian income tax purposes. It is your opinion that the contributions will not be taxable currently in Canada if you make an election under paragraph 7 of Article XVIII of the Canada-U.S Income Tax Convention (the "Convention").

If your contributions are not deductible for Canadian income tax purposes, you have asked how it would be possible to avoid double taxation when these amounts are ultimately distributed to you from an annuity.

Our Comments

Paragraph 7 of Article XVIII of the Convention reads as follows:

7. A natural person who is a citizen or resident of a Contracting State and a beneficiary of a trust, company, organization or other arrangement that is a resident of the other Contracting State, generally exempt from income taxation in that other State and operated exclusively to provide pension, retirement or employee benefits may elect to defer taxation in the first-mentioned State, under rules established by the competent authority of that State, with respect to any income accrued in the plan but not distributed by the plan, until such time as and to the extent that a distribution is made from the plan or any plan substituted therefor.

As stated in paragraph 7 of Article XVIII of the Convention, the election is only in respect of "income accrued in the plan, but not distributed by the plan." Consequently, this paragraph of the

Convention does not address the issue as to the taxability of amounts contributed by you to the U.S. resident pension plan for Canadian tax purposes.

Because the pension plan is a foreign plan, there is no deduction available to you for Canadian income tax purposes for your contributions to the plan. These contributions must be added back for each taxation year (to your W-2 income) in computing your income from employment for Canadian tax purposes.

For Canadian income tax purposes, we consider your 403(b) plan to be an "employee benefit plan". Consequently, payments received by you are to be included in income for Canadian tax purposes under paragraph 6(1)(g) of the Income Tax Act except for the payments that can be reasonably considered to be a return of amounts which you contributed to the plan. As stated in paragraph 19 of Interpretation Bulletin 502 entitled Employee Benefit Plans and Employee Trusts, payments from an employee benefit plan are considered to be first a return of EBP beneficiary contributions, secondly a distribution of the plan's income for the year, thirdly a distribution of employer contributions and finally a distribution of the plan's prior years' income, if any.

We trust the foregoing comments are of assistance.

Your truly,

Patricia Spice
for Director
Financial Industries Division
Income Tax Rulings Directorate
Policy and Legislation Branch