

## Internal Revenue Service

Department of the Treasury

Number: **200111027**

Washington, DC 20224

Release Date: 3/16/2001

Index Number: 9114.03-06

Person to Contact:

Telephone Number:

Refer Reply To:

CC:INTL:Br1-PLR-130713-00

Date:

December 15, 2000

TY:

Corporation =

Trustee =

Dear :

This refers to our letter to Corporation dated February 21, 1991, in which we concluded that interest and dividend income from the United States derived by certain exempt Canadian pension funds and Canadian charitable organizations through a pooled investment fund is exempt from U.S. taxation under Article XXI, paragraph 2(b) of the U.S.-Canada Income Tax Treaty (the "Treaty").

Under the facts as originally submitted, Corporation is a corporation organized under the laws of Canada. Corporation is not engaged in a U.S. trade or business and has no permanent establishment in the United States. Corporation provides investment management services for pension funds, insurance companies, individuals, charitable and religious organizations, and mutual funds. Corporation manages both segregated client funds and a pooled investment fund ("Pooled Fund").

The Pooled Fund is organized under the laws of Canada. The Trustee of the Pooled Fund is an unrelated trust company. The Pooled Fund is segregated into 15 sections. Some of the sections invest or are permitted to invest in U.S. stocks and interest-bearing obligations ("U.S. sections"). Under the Pooled Fund's Pooled Trust Indenture ("Indenture"), interest and dividend income is the only U.S. source income that can be generated by the U.S. sections. For Canadian legal and tax purposes, each section of the Pooled Fund is considered to be a separate trust. No section of the Pooled Fund is engaged in the conduct of a U.S. trade or business and no section has a U.S. permanent establishment.

Under the Indenture, participation in the Pooled Fund is limited to: (1) trusts maintained with respect to a registered pension plan that are tax exempt under the Canadian

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Income Tax Act ("ITA"), Paragraph 149(1)(o); (2) trusts maintained with respect to a retirement or other employee benefit or profit sharing plan that are tax exempt under ITA, Paragraph 149(1)(o) or (p); or (3) tax-exempt persons, as defined under ITA, Paragraph 149(1)(1), including funds for hospitals, educational, religious, or other charitable institutions. All eligible participants qualify for an exemption from Canadian income tax. The Indenture allows all eligible participants to invest in the U.S. sections.

Although the Pooled Fund is potentially liable for Canadian income tax, it does not pay any Canadian tax because all of its income is currently distributed to its investors and it is entitled to a deduction for amounts distributed.

Section 894(a) of the Internal Revenue Code states that the provisions of the Code shall be applied to any taxpayer with due regard to any treaty obligation of the United States which applies to such taxpayer.

Article XXI (Exempt Organizations), paragraph 1 of the Treaty provides:

Subject to the provisions of paragraph 3, income derived by a religious, scientific, literary, educational or charitable organization shall be exempt from tax in a Contracting State if it is resident in the other Contracting State but only to the extent that such income is exempt from tax in that other State.

Article XXI, paragraph 2 provides:

Subject to the provisions of paragraph 3, income referred to in Articles X (Dividends) and XI (Interest) derived by:

(a) A trust, company, organization or other arrangement that is a resident of a Contracting State, generally exempt from income taxation in a taxable year in that State and operated exclusively to administer or provide pension, retirement or employee benefits; or

(b) A trust, company, organization or other arrangement that is a resident of a Contracting State, generally exempt from income taxation in a taxable year in that State *and operated exclusively to earn income for the benefit of an organization referred to in subparagraph (a)*;

shall be exempt from income taxation in that taxable year in the other Contracting State. (Emphasis added.)

Article XXI, paragraph 3, states that the provisions of paragraphs 1 and 2 shall not apply with respect to the income of a trust, company, organization or other arrangement from carrying on a trade or business or from a related person other than a person

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referred to in paragraph 1 or 2.

The legislative history of Article XXI(2)(b) indicates that it was intended to provide mutual exemption for organizations acting as conduits for tax exempt pension funds.

Article X (of the First Protocol amending the 1980 Tax Convention With Canada) amends Article XXI of the proposed treaty to make it clear that an entity used exclusively as a conduit to earn income *for an employee benefit plan or fund* is subject to the same treaty rules as an employee benefit plan or fund.

S. Rep. No. 98-22, at 51 (1984)(emphasis added).

The letter to Corporation, dated February 21, 1991, concludes that the interest and dividend income derived from the United States by the Canadian pension trusts and charitable trusts through the Pooled Fund is exempt from U.S. taxation under section 894(a) and Article XXI(2)(b) of the Treaty.

After reconsideration, we have concluded that interest and dividend income derived from the United States by a pooled fund that includes both Canadian pension trusts and charitable trusts is not exempt from U.S. taxation under Article XXI(2)(b) of the Treaty. A pooled fund that includes as an investor an organization not described in Article XXI(2)(a) is not entitled to benefits under Article XXI(2)(b).

The private letter ruling dated February 21, 1991, is revoked to the extent it is inconsistent with this conclusion. However, pursuant to the authority granted in section 7805(b) of the Code, this revocation will only apply to interest and dividends paid after January 1, 2002.

This ruling is directed only to the taxpayer that requested the original ruling and its successors. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,  
M. GRACE FLEEMAN  
Assistant to the Branch Chief, Branch 1  
Associate Chief Counsel (International)