

TAXATION FOR NON-REGISTERED SEGREGATED FUND CONTRACTS

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A segregated fund may earn interest, dividends, capital gains or losses, and foreign income. The segregated fund allocates all income and losses among contract owners who held units of the fund during the calendar year. These are allocated to contract owners at the end of each calendar year and reported on a T3 slip for non-registered contracts (or T3 and Relevé 16 for Quebec residents). For Sun Life Guaranteed Investment Funds (GIFs), allocations are time-weighted based on the number of months the client held the units during the year.*

How are mutual fund trust distributions and segregated fund allocations different?

Mutual fund trusts distribute taxable income and net realized capital gains to unit holders, but not capital losses. Capital losses are deducted from capital gains earned by the fund. Capital losses that exceed capital gains in the year are carried forward to offset future capital gains. Clients have the option to receive their distributions in cash or reinvest them in the fund. The unit value decreases by the amount of the distribution per unit. Clients don't receive distributions for units they've sold before the distribution date.

Segregated funds allocate taxable income and realized capital gains and/or losses to contract owners. A segregated fund allocates gains and/or losses first to clients who redeemed units. Allocations can't be paid in cash as they are with mutual fund distributions (a withdrawal request from the fund is required). Unit values don't change with an allocation and allocations can't be used to purchase additional units.

EXAMPLE:

MUTUAL FUND TRUST DISTRIBUTION					SEGREGATED FUND ALLOCATION			
	Net asset value per unit (NAVPU)	# of units	Market value	Adjusted cost base (ACB)	Unit value	# of units	Market value	ACB
BEFORE	\$10.00	10	\$100	\$100	\$10.00	10	\$100	\$100
MARKET VALUE = # OF UNITS/SHARES X UNIT/SHARE VALUE: 10 X \$10.00 = \$100.00								
AFTER A \$1.00 DISTRIBUTION PER UNIT:					AFTER A \$1.00 ALLOCATION PER UNIT:			
AFTER	\$9.00	11.1 – reinvested distribution buys 1.1 units (\$10.00/\$9.00)	\$100 (11.1 units x \$9.00)	\$110	\$10.00	10	\$100 (10 units x \$10)	\$110
IN BOTH INSTANCES, THE MARKET VALUE AFTER THE DISTRIBUTION OR ALLOCATION = \$100.00								

*There may also be additional capital gain/loss allocations at year-end due to trading activity of the fund.



DID YOU KNOW?

Clients could receive a T3 even if they didn't redeem any units during the year.

- Why? At year-end, the income earned in a segregated fund is allocated to unit holders and reported on a T3 slip (Relevé 16 for Quebec residents). Even if clients haven't redeemed units, they may earn income due to segregated fund allocations.

Clients may receive a T3 even if the market value of their segregated fund has declined.

- Why? The T3 reports income earned in a segregated fund as well as realized capital gain or loss from the sale of units. The decline in market value of the segregated fund year over year represents an unrealized capital loss if the units of the fund haven't been sold. Unrealized gains or losses aren't included in the T3.

Clients could have a segregated fund loss reported on their T3 even if their year-end statement shows market growth for the year.

- Why? A loss occurs if the cost of assets sold by the segregated fund during the year is greater than their market value on the date they're sold. These capital losses within the segregated fund are allocated to unit holders, which are then reported on the T3 so clients can claim the loss on their income tax return. Even if clients haven't redeemed units during the year, their allocated share of the capital losses from activity within the fund is reported.

TAX TREATMENT OF INCOME

Different types of income receive different tax treatment. The table below shows the tax treatment for the types of income segregated funds may earn and where they're reported on a T3 slip.

TYPE OF INVESTMENT/FUND-LEVEL ACTIVITY	INCOME EARNED	HOW IS IT TAXED?	WHERE IS THIS INCOME REPORTED ON T3?
Canadian treasury bills and bonds	Interest	Interest is fully taxed as income at a client's marginal tax rate.	Box 26
Foreign bonds/shares of foreign corporations	Foreign income	In Canada, the interest and dividends from foreign bonds are fully taxed as income. In cases where a foreign jurisdiction also taxes the income, this is done before the income is allocated to clients.	Box 25
Shares of Canadian corporations	Dividends	A dividend tax credit applies to dividends. The dividend tax credits for eligible and non-eligible dividends are reported in boxes 51 and 39 respectively.	Box 49 or box 23 (actual amounts) Box 50 or box 37 (taxable amounts)
Fund manager sells investments owned by the segregated fund	Capital gain or loss	Capital gains receive preferential tax treatment. A client only has to include 50% of that gain in their income.	Box 21 or box 37
Client redeems units in the segregated fund contract	Capital gain or loss	When a client redeems units from a segregated fund contract, a capital gain is reported if the market value is greater than the adjusted cost base (ACB). A loss is reported if the market value is lower than the ACB. Guarantee top-ups at maturity or upon the death of the annuitant are reported as a capital gain.	Box 21 or box 37

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