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## INTERNATIONAL TAX PLANNING

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### FOREIGN AFFILIATES: TRACING THE PURPOSE AND USE OF FUNDS

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Tracing the purpose and use of funds is fundamental in determining the ability of a taxpayer to deduct interest on a debt. Various judicial decisions regarding interest deductibility have commented on the practice of tracing, prompting the Canada Revenue Agency to publish its administrative practices. Numerous foreign affiliate rules that relieve a taxpayer from imputed income contain purpose-and-use tests as conditions for their application. This article describes the tracing requirements for certain foreign affiliate provisions, and demonstrates how interest-tracing concepts can be applied to support the purpose and use of funds by a foreign affiliate.

**KEYWORDS:** FOREIGN AFFILIATES ■ INTEREST DEDUCTIBILITY ■ FAPI ■ SOURCES ■ PURPOSE

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