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UNDERSTANDING FOREIGN WITHHOLDING TAX

A reference guide

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Exchange-traded funds make it easier than ever before to gain diversified, low-cost exposure to international markets, but for all the benefits that investing abroad offers, Canadian investors need to be aware of the potential withholding tax being charged on their foreign ETF investments alongside other cost considerations such as foreign exchange and management and trading expenses.

While most countries impose some level of withholding tax on dividends paid to foreign investors, the exact amount that Canadian ETF investors are required to pay can vary depending on geography and asset class, as well as the structure of the exchange traded fund and whether or not the ETF is held in a taxable or non-taxable investment account.

In some instances, Canadian investors with foreign exposure may pay no withholding tax; in other instances, they may be subject to multiple layers of withholding tax.

No matter the circumstance, it's important to remember that withholding tax is only one consideration of many in the decision to invest abroad. When choosing which product to use, tax implications should be weighed against other product features, such as the investment strategy of the fund, its overall liquidity and management fees.

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Here are some key points to help better understand the potential impact of foreign withholding tax on your international investments:

U.S. Stock Exposure

- All Canadian listed ETFs or mutual funds seeking exposure to equities south of the border are subject to the same level of withholding tax regardless of whether the ETF invests directly in U.S. stocks, or indirectly via a U.S. or another Canadian ETF. This withholding tax will apply regardless of whether the investor holds the Canadian ETF product in a taxable or non-taxable account.

- Canadian and U.S.-listed ETFs held in a taxable account are generally eligible for tax credits that can reduce the effect of withholding tax paid.

- Investors are generally exempt from U.S. withholding tax when they hold U.S. listed ETFs or U.S. stocks directly in a Registered Retirement Saving Plan (RRSP) or Registered Retirement Income Fund (RRIF).

International Stock Exposure

- All Canadian-listed ETFs seeking exposure to international stocks are generally subject to foreign withholding tax levied by the jurisdiction of incorporation of the stock issuer (e.g., Japan charges withholding tax on Japanese stocks in the ETF, Germany charges withholding tax on German stocks in the ETF...)

- Canadian-listed ETFs that invest in international stocks indirectly through a U.S. ETF may be required to pay U.S. and foreign withholding tax resulting in two layers of taxation. However, the fund-of-fund structure generally leads to lower trading costs.

- Investors can also consider U.S. listed ETFs that hold international stocks directly. Such products are generally subject to foreign (non-U.S.) withholding tax. U.S. withholding tax may or may not apply, depending on whether the U.S. ETF is held in a taxable account or not.

U.S. Bond Exposure

- All Canadian-listed ETFs seeking exposure to U.S. bonds are generally exempt from the U.S. withholding tax on qualified interest income, regardless of whether or not the ETF is held in a taxable or non-taxable investment account.

What do you pay?

The U.S. withholding tax rate charged to foreign investors on U.S. dividends is 30%, but this amount is generally reduced to 15% for taxable Canadian investors by a tax treaty between the U.S. and Canada.

The withholding tax rates for international stocks vary by country. For illustration, The weighted average foreign withholding tax rate on international stocks represented by the MSCI EAFE Index is 11.44%.[1]

1 Source: MSCI, BlackRock, as of August 31, 2023. Calculated based on the respective country weights in the MSCI EAFE Index and their corresponding MSCI country index dividend yield, along with specific country treatment of withholding tax. Subject to change.

Foreign withholding tax quick guide

Exposure	Structure	RRSP and RRIF	
		U.S. withholding tax	Foreign withholding tax
U.S. Stocks	Direct securities	Exempted	N/A
	U.S. ETF	Exempted	N/A
	Canadian MF or ETF:		
	• Holds U.S. stocks	WHT applies, net cost	N/A
	• Wraps CDN ETF holding U.S. stocks	WHT applies, net cost	N/A
	• Wraps U.S. ETF holding U.S. stocks	WHT applies, net cost	N/A
International Stocks	Direct securities	N/A	WHT applies, net cost
	U.S. ETF	Exempted	WHT applies, net cost
	Canadian MF or ETF:		
	• Holds international stocks	N/A	WHT applies, net cost
	• Wraps CDN ETF holding international stocks	N/A	WHT applies, net cost
	• Wraps U.S. ETF holding international stocks	WHT applies, net cost	WHT applies, net cost
U.S. Bonds*	Direct securities	Exempted	N/A
	U.S. ETF	Exempted	N/A
	Canadian MF or ETF:		
	• Holds U.S. bonds	Exempted	N/A
	• Wraps U.S. ETF holding U.S. bonds	Exempted	N/A

* Assuming all income generated is qualified interest income

RRSP: Registered Retirement Savings Plan
RRIF: Registered Retirement Income Fund

TFSA: Tax-Free Savings Account
RESP: Registered Education Savings Plan

TFSA and RESP		Taxable	
U.S. withholding tax	Foreign withholding tax	U.S. withholding tax	Foreign withholding tax
WHT applies, net cost	N/A	WHT applies, creditable	N/A
WHT applies, net cost	N/A	WHT applies, creditable	N/A
WHT applies, net cost	N/A	WHT applies, creditable	N/A
WHT applies, net cost	N/A	WHT applies, creditable	N/A
WHT applies, net cost	N/A	WHT applies, creditable	N/A
N/A	WHT applies, net cost	N/A	WHT applies, creditable
WHT applies, net cost	WHT applies, net cost	WHT applies, creditable	WHT applies, net cost
N/A	WHT applies, net cost	N/A	WHT applies, creditable
N/A	WHT applies, net cost	N/A	WHT applies, creditable
WHT applies, net cost	WHT applies, net cost	WHT applies, creditable	WHT applies, net cost
Exempted	N/A	Exempted	N/A
Exempted	N/A	Exempted	N/A
Exempted	N/A	Exempted	N/A
Exempted	N/A	Exempted	N/A

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