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CC:PA:LPD:PR (NOT-121556-10)  
Room 5203  
Internal Revenue Service  
P.O. Box 7604, Ben Franklin Station  
Washington DC 20044

**VIA EMAIL TO: [Notice.Comments@irscounsel.treas.gov](mailto:Notice.Comments@irscounsel.treas.gov) (NOT-121556-10)**

**Re: IRS Notice 2011-34 “Supplemental Notice to Notice 2010-60 Providing Further Guidance and Requesting Comments on Certain Priority Issues Under Chapter 4 of Subtitle A of the Code” (the Notice)**

Dear Sirs/Madam:

The Investment Industry Association of Canada (**IIAC**) is writing this letter to the Department of the Treasury (**Treasury**) and the Internal Revenue Service (**IRS**) in response to the request for comments on the guidance provided in the Notice, and on other priority issues that should be addressed in future guidance and regulations.

**WHO WE ARE**

The IIAC is Canada’s equivalent to the Securities Industry and Financial Markets Association (**SIFMA**) in the United States, and represents approximately 95% of all investment dealers across Canada - 189 bank-owned and independent firms in total. Our members provide a variety of financial services including, but not limited to, the following:

- Full service brokerage
- Discount brokerage
- Discretionary investment management
- Institutional custody

Most of our larger members (based on number of account holders and assets under administration) are part of global groups of financial institutions that offer a diversified range of services worldwide. Our members manage over \$900 billion in assets for their clients in 9.8 million brokerage accounts.<sup>1</sup> Products offered by our members include equity securities (common and preferred stock) and fixed income securities (including bonds, treasury bills, commercial paper and bankers' acceptances), mutual funds, and more sophisticated instruments such as options, futures or other risk management products.

### ***Introduction***

The IIAC appreciates that changes to the proposals in Notice 2010-60 were made in response to comments submitted by our association and other organizations. However, we have some very serious concerns with respect to some of the proposed concepts in the Notice that we believe do not strike a reasonable balance between the policy goals of FATCA<sup>2</sup> and the administrative burden to be placed on foreign financial institutions (**FFIs**) – particularly in the areas of private banking and passthru payments. We describe these concerns in sections 1 and 2 of this letter.

Our members have also raised concerns with respect to a portion of the Notice dealing with cost basis reporting, which has caused confusion among firms who are currently implementing systems and procedures to comply with the basis reporting regulations for the 2011 tax reporting season. These concerns are briefly described in section 3 of this letter, and more fully in the letter to Treasury and the IRS dated May 4, 2011, attached as Appendix "A" hereto.

### ***Comments on Notice 2011-34***

#### ***1. Revised Procedures for Identification of Preexisting Individual Accounts***

The IIAC appreciates and welcomes some of the changes that were made to the proposed procedures for identifying U.S. accounts among preexisting individual accounts, including the following:

- Recognition of limits on the sharing of account holder information across FFI branches or affiliates located in different jurisdictions because of legal restrictions and because of certain limitations of many FFIs' information technology systems.
- Reconsideration of the treatment of non-U.S. P.O. boxes as an indication of U.S. status.

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<sup>1</sup> More information and a list of members is available at <http://www.iiac.ca>.

<sup>2</sup> The Foreign Account Tax Compliance provisions contained within Title V, Subtitle A of the *Hiring Incentives to Restore Employment (HIRE) Act*.

- Clarification of the terms “electronically searchable information”, “documentary evidence” and “documentation” and flexibility to maintain copies or records of documentary evidence examined.
- Reconsideration of the application of new individual account identification procedures described in Notice 2010-60 to preexisting individual accounts.
- Option to treat all preexisting accounts with balances not exceeding \$50,000 as non-U.S. accounts.

However, we have a number of new concerns about the revised procedures for identification of preexisting individual accounts as described in section I.A of the Notice which we believe will misdirect FFI resources toward conducting manual due diligence on the files of accountholders who present a low-risk of U.S. tax evasion, without any electronic pre-screening for U.S. indicia.

In general, while we support the concept of applying a targeted, risk-based approach to the identification of U.S. accountholders among preexisting individual accounts, we continue to disagree with the adoption of any approach that requires the manual search of paper or electronic files (i.e. any due diligence that cannot be conducted by an automated electronic search). ***We strongly recommend that in the interest of accuracy and efficiency, that Treasury and the IRS reconsider the proposed procedures in the Notice that would require “diligent reviews of the paper and electronic account files and other records” as suggested in sections I.A.2. Step 3 “Private Banking Accounts” and Step 5 “Accounts of \$500,000 or More”. We respectfully suggest that the searches conducted with respect to these targeted accounts should be limited to automated electronic searches for U.S. indicia with follow up for additional due diligence and/or documentation where U.S. indicia is present.*** We feel particularly strongly that FFIs that are already Qualified Intermediaries (QIs), and have been tracking U.S. indicia and collecting the required documentation for all accounts as part of their standard account opening procedures, should be allowed to search preexisting accounts electronically.

However, in the event that Treasury and the IRS ultimately conclude that some form of manual due diligence is required with respect to initial searches of targeted subsets of accounts, we have provided further comments below.

#### ***A. Definition and Obligations with respect to Private Banking Accounts***

In the Notice, a “private banking account” is defined as “any account maintained or serviced by an FFI’s *private banking department* or any account maintained or serviced as part of a *private banking relationship...*” (*emphasis added*)

A “private banking department” is defined as any department, unit, division, or similar part of an FFI:

(A) that is referred to by the FFI as private banking, *wealth management*, or similar department;

(B) that focuses on servicing accounts and investments of individual clients (*or their families*) whose accounts with the FFI or whose income, earnings, or assets exceed certain thresholds, or who are otherwise identified as high-net worth individuals (*or families*), as determined under an FFI's own policies and procedures;

(C) that is considered a private banking department under the anti-money laundering or know-your-customer (**AML/KYC**) requirements to which the FFI is subject; or

(D) in which some of all of its employees, under any of an FFI's formal or informal procedures or other guidelines for its personnel: (i) ordinarily provide *personalized services* to individual clients (*or their families*), such as *banking, investment advisory, trust and fiduciary, estate planning, philanthropic, or other services* not generally provided to account holders; or (ii) *gather information about individual clients' personal, professional, and financial histories* in addition to the information ordinarily gathered with respect to the FFI's retail customers. (*emphasis added*)

**Definition of "private banking":** The definitions of "private banking account" and "private banking relationship" are extremely broad, and when applied to the accounts of IAC members, would include accounts that are neither high net-worth accounts nor at a high-risk for tax evasion. By including all-encompassing terms that may be interpreted differently by FFIs, such as "wealth management" or "investment advisory" services, the definition of private banking in the Notice could potentially include all securities accounts, including discount brokerage accounts for some financial institutions, excluding only basic accounts without any level of advisory services.

Preliminary estimates by our largest brokerage member firms show that approximately 70% - 100% of all of their accounts could be included under the overly broad Notice definition of "private banking" as compared to 5% - 10% of accounts that are currently designated as true "private client" or "private banking" division accounts.

We are concerned that efforts put toward identifying U.S. persons among preexisting accounts using the broad definition in the Notice will actually misdirect efforts and resources toward accounts that are neither high-risk nor high net-worth. For example, a client may receive personalized services or financial planning and advice, and may provide detailed information about personal, professional or financial history, and yet

may not be considered a “high net-worth” individual. Under the proposed Notice, these individuals may be targeted for manual due diligence. According to our estimates, these individuals could make up a large percentage of firm accounts, misdirecting resources that could otherwise be made available for searches and follow-up due diligence with respect to accounts belonging to high net-worth and high-risk individuals.

***We do not recommend redrafting the definition to narrow or clarify it, as it may be difficult to define “private banking” in a manner that works for all industry segments in all jurisdictions; we believe that the policy goals of FATCA would be better achieved by removing the definitions associated with “private banking” and Step 3 of the proposed identification procedures to instead focus on conducting due diligence with respect to accounts that exceed a designated threshold amount (see recommendation below with respect to threshold levels).***

***Families:*** The proposed definitions for identification of U.S. persons in preexisting accounts, and Step 3 of the procedures, includes language that implies obligations to expand due diligence to the families of individual clients. However, it is not clear to what extent family members would be implicated by indicia of U.S. status with respect to a preexisting account holder and vice versa. ***We request further clarification on this point, and recommend that family members of account holders only be included in the identification process where the client has taken steps to link the account to a family member.*** It is important to note that FFIs will only have the documentation on file in searchable format for family members where the accounts are actively tagged and linked.

***Responsibility for Searches and Due Diligence:*** Section I.A.2 Step 3 proposes that with respect to private banking accounts, “the FFI must ensure that all of the FFI’s private banking relationship managers...perform a diligent review of the paper and electronic account files and other records for each client with respect to whom they serve as a private banking relationship manager”, with further associated proposed responsibilities to identify each client with U.S. indicia, and to request documentation from identified clients to establish whether the client’s account is a U.S. account.

If Treasury and the IRS maintain the view that manual due diligence of certain preexisting account files is required to identify U.S. persons (beyond electronic searches), we do not believe that such due diligence can effectively or efficiently be carried out at the relationship management level at most securities dealers in Canada. Currently, AML and KYC documentation paperwork are administered at the relationship level, however, it is our understanding that all documentation is centrally stored and located, and vetted for approval centrally by compliance personnel. This is particularly true for securities dealers associated with large affiliated financial groups, something that is recognized in the Notice in the sections dealing with FFI Agreement execution

and the proposed centralized compliance option.

Centralized compliance and tax personnel will have the required knowledge of U.S. indicia and documentary evidence. Also, search and due diligence requirements may be less effective where FFIs experience turnover of relationship managers, a frequent occurrence among large FFI groups.

***We recommend that future guidance and regulations provide flexibility for firms to determine which internal personnel will carry out the required searches and due diligence, and specifically not to require this due diligence to be carried out at the relationship management level.*** For example, in Step 5 of the procedures dealing with the diligent review of accounts of \$500,000 or more, it is proposed that the “FFI must perform a diligent review of the account files”, without specifying personnel to carry out the review. We recommend that this general approach be taken with respect to any such reviews and follow up. FFIs would be required to certify the searches they conduct as proposed in the Notice, and as such, should be able to conduct these searches in an efficient and effective manner suited to internal organization and business models.

#### ***B. Obligations with respect to accounts based on size thresholds***

As mentioned in a previous section of this submission, the IIAC believes that a targeted approach to identifying U.S. persons among preexisting accountholders is a more effective and efficient way of carrying out the policy objectives of FATCA. We maintain that automated electronic searches of account files is the best way to balance the costs of implementation with the policy objectives, and we urge Treasury and the IRS to limit searches of preexisting accounts to electronic searches.

***However, if Treasury and the IRS require enhanced manual due diligence with respect to non-electronically searchable account documentation, we recommend that Step 3 of the proposed procedures (“private banking accounts”) either be removed altogether or combined with Step 5 (“accounts of \$500,000 or more”) in a way that would ensure that the only accounts subject to manual due diligence are clearly defined as accounts that exceed a certain threshold dollar amount. We also recommend that this threshold dollar amount be raised to \$1 million dollars, following the precedent set in the definition of “private banking account” in the USA Patriot Act.<sup>3</sup>*** This would satisfy the policy objective of targeting only accounts of high net-worth and high-risk individuals, and do so in an efficient and standardized fashion. It would remove subjectivity with respect to FFIs around the world in their interpretation of “private banking accounts”.

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<sup>3</sup> *International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001* [title III, § 301 et seq., of the *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT ACT)*, Pub. L. No. 107-56 (Oct. 12, 2001) at (§ 312(a)(i)(4)(B)).

### ***C. Aggregation of accounts***

Section I.A.2 of the Notice proposes that “for purposes of determining the balances or values (as relevant) of accounts...an FFI will be required to treat as a single account all accounts maintained by the FFI or its affiliates that are associated with one another due to partial or complete common ownership of the accounts under the FFI’s *existing computerized information management, accounting, tax reporting, or other recordkeeping systems.*” (*emphasis added*)

Our members have indicated that in instances where existing reporting infrastructure can currently track accounts within business lines, the infrastructure does not necessarily exist for these account balances to be combined and aggregated.

***We would appreciate further clarification to confirm that FFIs are only obligated to aggregate accounts to the extent that those capabilities currently exist, and to search and report separately on non-aggregated accounts where they do not.***

In addition, we have been provided with feedback from our member firms, confirming that in almost all cases, aggregation could only be achieved through the use of Canadian Social Insurance Number (**SIN**) searches. Uses of the SIN are limited by legislation, and consequently, many securities dealers and other financial institutions have standard privacy policies in place to use SIN only for these legislated purposes. We have included for your information an abbreviated version of the SIN “Fact Sheet” provided by the Office of the Privacy Commissioner (Canada), attached as Appendix “B” hereto.

***We would appreciate confirmation that FFIs are not obligated to aggregate accounts where the only means by which to identify common ownership is by searching SIN.***

### ***D. Certifying Completion of Customer Identification Procedures***

The Notice proposes that the chief compliance officer or another equivalent-level officer of the FFI (a **responsible officer**) must certify to the IRS when the FFI has completed the proposed procedures with respect to preexisting individual accounts. As part of these certifications, the responsible officer will be required to certify (along with certification of completion of the Steps for identification proposed by the Notice) that:

- Between the publication date of the Notice and the effective date of the FFI’s FFI Agreement, FFI management personnel did not engage in any activity, or have any formal or informal policies and procedures in place, directing, encouraging, or assisting account holders with respect to strategies for avoiding identification of their accounts as U.S. accounts under the proposed procedures; and

- That the FFI had written policies and procedures in place as of the effective date of the FFI's FFI Agreement prohibiting its employees from advising U.S. account holders on how to avoid having their U.S. accounts identified.

While we do not disagree with the concept of certification of compliance with agreed upon procedures and the adoption of written policies and procedures, we believe that portions of the proposed certification require attestation that would go beyond the knowledge and control of the responsible officer. For example, while a responsible officer could certify as to the completion of required searches and the development of internal procedures prohibiting their employees from engaging in avoidance behaviour, it would be practically impossible for the responsible officer to certify that employees had not engaged in this kind of behaviour, especially on a retroactive basis (to the date of the Notice's publication). ***As such, we recommend that this portion of the certification component (certifying that management personnel did not engage in avoidance behaviour) either be removed in its entirety, or at a minimum, removing the retroactive aspect of the certification and including a "knowledge" qualifier.***

#### ***E. Long Term Recalcitrant Account Holders***

We reiterate our position from our previous submission that it seems unreasonable to terminate an FFI's FFI Agreement for reasons beyond the control of the FFI, such as non-responsiveness by a recalcitrant account holder to a request for information. ***Because of this, and also because of the fact that FFIs will be documenting and withholding on any passthru payments made to a recalcitrant accountholder, we believe that termination of an FFI Agreement would be a heavy-handed and unnecessary sanction on the part of the IRS, possibly with unforeseen consequences that could cascade through a chain of FFIs.*** FFIs can best determine based on their business models what actions they would like to take and whether they wish to maintain business relationships and accounts with non-participating FFIs and recalcitrant account holders.

#### ***F. Timing of Completion of Preexisting Account Identification Process***

The Notice proposes that procedures under Section I.A.2. Step 3 (Private Banking Accounts) must be completed "*by the end of the first year in which an FFI's FFI Agreement is in effect*" and also proposes that non-compliant account holders be treated as recalcitrant accounts holders "*after the end of the first year in which the FFI's FFI Agreement is in effect*". This language has been interpreted by some of our members to mean that less than one full year is being provided to complete these steps, instead of one full year from the effective date of the FFI Agreement – which we believe may not be the interpretation that was intended.

***We recommend that Treasury and the IRS clarify in all instances of one-year time***

***limits that these limits run from the effective date of the FFI Agreement, and not according to a calendar year-end.*** For example, in Step 4 (Accounts with U.S. Indicia), language is used to propose that certain requests are to be made “*within one year of the effective date of the FFI’s FFI Agreement*”. We suggest that this language be used in all cases where requirements must be carried out within one year of the effective date of the FFI Agreement, in order to remove any ambiguity with respect to the interpretation.

## **2. Passthru Payments**

### **A. General comments**

We understand that Section 1471(b)(1)(D) of the FATCA legislation requires a participating FFI to deduct and withhold a tax equal to 30% of any “passthru payment” made to a recalcitrant account holder or non-participating FFI, and that “passthru payment” is defined as “any withholdable payment or other payment to the extent attributable to a withholdable payment”. While we understand the policy objective of Treasury and the IRS to discourage the use of participating FFIs as “blockers” through which non-participating FFIs might indirectly invest in U.S. assets, we respectfully disagree with the approach taken in the Notice with respect to the determination of passthru payment percentages (**PP%**) and believe that the policy goal of deterrence could be achieved without the excessive administrative burden we foresee connected with the passthru payment concept proposed in the Notice. The current Notice would place an extremely large burden upon compliant FFIs, when it should be more appropriately borne by the non-compliant accountholders and FFIs.

### **B. Administration of Passthru Payments**

We suspect that the proposed approach to passthru payments in the Notice has been developed to address concerns of the fund industry with respect to the administrability of a tracing approach for passthru payments. However, we have concerns that the proposed approach will not be appropriate or administrable for securities dealers or other FFIs (such as banks) in Canada (or elsewhere) where FFIs are engaged in active business, and ***where a calculation of the FFI’s U.S. assets at a particular moment in time may not be an appropriate indicator of indirect investment in the U.S.*** For example, a Canadian fund may invest in U.S. based companies as part of its portfolio of investments (and appropriately disclosed as such in required documentation), therefore making a PP% an appropriate proxy for indirect U.S. investment; however, a Canadian bank may own various U.S. assets, but it would be an illogical step to conclude that a shareholder in that bank intended to invest indirectly in U.S. assets, especially when those assets may not be fully disclosed to the shareholder. In that instance, PP% as described in the Notice would not be an appropriate proxy for indirect U.S. investment,

and becomes a more arbitrary number – and one that requires a great deal of administrative cost to calculate.

Those of our members who have attempted the process of estimating their passthru payment percentages according to the general instructions in the Notice have provided us with preliminary feedback that the calculation is too complex to be completed on quarterly testing dates. We have also received feedback that the instructions provided in Sections II.B.3 (“Determination of Assets” and 4 (“Definition of U.S. Asset”) are too vague, and that a great deal of resources (of the Treasury, IRS and FFIs) would be required to develop future guidance to ensure that FFI interpretations of what assets are to be included in the calculations are consistent and easily understood.

We also question the relevance and validity of the PP% calculated by FFIs, given that many FFIs have significant ownership holdings in other FFIs. Initial attempts at calculation by our members show that these circular holdings can create skewed results and wild fluctuations in PP% from quarter to quarter, which makes the PP% a very poor indicator of indirect investment in the U.S.

The complex nature of the passthru payment definition and the calculation of the PP% means that it will be almost impossible to explain to a recalcitrant account holder why a withholding was made on investment (particularly if the investment is in a non-U.S. FFI), and how the withholding was calculated. Our members are concerned about client service issues, and anticipate legal challenges made by Canadian accounts holders who hold Canadian FFI investments who discover that a portion of their income or proceeds on these investments has been withheld and remitted to U.S. tax authorities – without any basis for doing so under Canadian tax law or the Canadian – U.S. tax treaty, and potentially without permission under existing contracts that account holders have entered into with the FFI. The Canadian financial industry has not yet fully investigated these legal risks, and the IIAC will be discussing them with the Canadian Department of Finance in June.

Finally, we have many concerns about how information can be disseminated on a reliable basis to implement the passthru payment regime. In addition to the observation that the publication of PP% is requiring FFIs to publish what could essentially be competitive information about their operating entities in the U.S., it has also been suggested by many that the only reliable list or database of participating or deemed compliant FFIs (and their PP%) is one that would be maintained by the IRS. Members question the reliability of third-party feeds and sources of information, especially given that so much relies on the veracity of information about other FFIs. FFIs would only feel comfort if the information has in fact been vetted and provided by the IRS.

### **C. Recommendations**

As articulated above and in our previous submissions, we believe that passthru payments should only apply to withholdable payments where the payment is directly traceable to the client's investment in the U.S., a concept that is more administratively feasible for securities dealers who engage in active business. The portion of the passthru payment that requires the calculation of PP%, applicable to non-withholdable payments, is not practical in its administration, nor does it seem to be a good indicator of indirect investment in the U.S. The concept of "passthru payment" should only be applied to payments flowing through custodial accounts, where the FFI can look through to the underlying investment. FFIs should not be calculating PP%, but should instead be treated in essentially similar fashion (with respect to non-custodial payments) like any other operating non-financial foreign entity.

We understand that Treasury and the IRS are concerned about participating FFIs that could be used as "blockers" through which non-participating FFIs might benefit from indirect investment in U.S. assets; however, we do not believe that the passthru payment concepts outlined in the Notice will be effective in addressing this concern, and that for FFIs that have active operating businesses, the costs and complexity will outweigh the benefits.

Finally, we believe that the resources and efforts that are being focused on passthru payments may have the unintended consequence of delaying the entire FATCA implementation. It will be more important for Treasury and the IRS to focus its efforts over the next 12-18 months on the rules necessary for successful implementation of the search and documentation portion of FATCA. After initial implementation of search and documentation, FFIs, Treasury and the IRS will know how many non-participating FFIs exist, and FFIs will know how many recalcitrant accounts require reporting and withholding.

***As such, we strongly recommend that Treasury and the IRS consider deferring any further guidance or regulations implementing the non-withholdable portion of the passthru payment, including the PP%, until the portions of FATCA dealing with the identification of U.S. persons, documentation and reporting have been finalized. A phased-in approach will allow Treasury, the IRS and FFIs to develop strategies for dealing with any non-participating FFIs or recalcitrant account holders in ways that are effective and administrable for different segments of the financial industry.***

### **3. Cost Basis Reporting Requirements and FATCA**

Section IV.C of the Notice states that "Treasury and the IRS intend to issue guidance providing that FFIs that are not U.S. payors (as defined in §1.6049-5(c)(5)) and that

report the information required under section 1471(c)(1)(D) with respect to a U.S. account will not be required to report tax basis information required under section 6045(g) with respect to the account.”

This section indicates that an FFI that is a non-U.S. payor and that enters into an FFI Agreement with the IRS and performs the required reporting under the FFI Agreement will not be required to perform cost basis reporting.

Based on the information in the Notice, FFIs that are non-U.S. payors that enter into an FFI Agreement with the IRS will not be required to report cost basis information. Since all QIs will be required to enter into an FFI Agreement, it appears that QIs that are non-U.S. payors and that perform the required reporting should be exempt from cost basis reporting.

While the Notice appears to provide for a complete exemption, Canadian QIs are concerned that it is only a statement of intent, and that ultimately, the scope of the exemption may be more narrow than that necessary to provide for a complete exemption from cost basis reporting. When the cost basis regulations were released, a general statement was made that non-U.S. payor QIs were exempt from cost basis reporting. However, a closer reading of the Treasury Regulations revealed a narrow exception to this rule that resulted in Canadian QIs being unable to make use of the exemption.

***Accordingly, the Canadian QI community would welcome an immediate and clear statement from Treasury and the IRS that the FATCA regulations will ultimately completely exempt QIs that are non-U.S. payors from the cost basis reporting requirements and that such exemption will apply retroactively to January 1, 2011 (as basis reporting is applicable to certain securities purchased on or after January 1, 2011).***

#### **4. Retirement Plans**

Section III.D. of the Notice reiterates the intention of Treasury and the IRS to issue guidance providing that “certain foreign retirement plans pose a low risk of tax evasion under section 1471(f), and therefore payments beneficially owned by such retirement plans will be exempt from withholding under section 1471(a).” In addition, “Treasury and the IRS intend to provide further guidance on foreign retirement plans or retirement accounts that may be deemed compliant under section 1471(b)(2).”

We are deeply concerned by these remarks, and the implication that individual retirement accounts are (a) being characterized as FFIs, and would be subject to all reporting and passthru payment requirements proposed for FFIs, and (b) that Treasury

and the IRS are considering completely disregarding the exemption from U.S. tax granted to registered retirement accounts under the Canada-U.S. income tax treaty.

Our previous detailed comments about registered Canadian savings plans are attached to this submission as Appendix "C". However, we strongly urge Treasury and the IRS to continue to consider our specific recommendations, and to ensure that individual savings accounts are not mis-characterized as FFIs under FATCA:

- 1. Given the regulatory restrictions attached to registered savings accounts and the degree of the monitoring by the Canadian Revenue Agency to which they are subject, the IIAC recommends that they also be excluded from either the definition of FFI or from the definition of U.S. account on the basis that they present a low risk of being used by U.S. persons for tax evasion.***
- 2. The IIAC recommends the exclusion from the definition of FFI and/or U.S. accounts all Canadian entities or accounts that are covered by Article XXI of the Canada – U.S. Treaty.***
- 3. It may be efficient for Treasury and the IRS to contemplate drafting regulations that would exclude from the definitions of FFI and/or U.S. account, all entities that are similarly covered under the tax treaties that have been negotiated between the U.S. and other countries. This would provide a global approach to the exclusion, as it could be applied to every country that has a tax treaty with the U.S. It is our understanding that a number of international financial associations have provided Treasury and the IRS with examples of how this might be accomplished, and the IIAC supports this general approach.***

### ***Conclusion***

In our previous submissions, we have consistently expressed our concerns about the ability of FFIs to implement FATCA requirements by the legislated effective date of January 1, 2013. We have consistently stated that our members believe that implementation will require 18-24 months of work after the release of final regulations. As of the date of this submission, the FATCA deadline of January 1, 2013 is only 18 months away. We have serious concerns, given the complex nature of the proposals in the current Notice and other outstanding issues, that FATCA cannot be implemented by the legislated effective date.

While we appreciate the efforts of Treasury and the IRS to engage the worldwide financial community through the notice and comment process, we urge policymakers to use more interactive approaches to deal with the complex concepts, such as passthru payments, perhaps in the form of industry working groups or workshops. In the

meantime, we urge Treasury and the IRS to use its authority wherever possible to extend the timeframe for implementation and to provide FFIs (and their clients) with safe harbour from penalties where they are demonstrating reasonable efforts to implement the FATCA requirements in good faith.

We appreciate the opportunity to provide our comments on the Notice. If you would like to engage in further discussion of these matters, please contact the undersigned or Andrea Taylor at [ataylor@iiac.ca](mailto:ataylor@iiac.ca) (416-687-5476).

Yours sincerely,



Ian Russell  
President and CEO  
IIAC

Cc: Michael Danilack, Deputy Commissioner (Int'l) LB&I, Internal Revenue Service  
Manal Corwin, Deputy Assistant Secretary Tax Policy (Int'l), Department of the Treasury  
Steven A. Musher, Associate Chief Counsel (Int'l), Internal Revenue Service  
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## APPENDIX "A"



Andrea Taylor  
Director

May 4, 2011

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Office of the International Tax Counsel  
U.S. Dept. of Treasury

John Sweeney  
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### ***SENT VIA EMAIL***

**Re: Urgent Request for Clarification of the Requirement for a Qualified Intermediary that is a Non-U.S. Payor to Report a Customer's Basis in Securities**

Dear Sirs/Madam:

We are writing on behalf of our members who are Qualified Intermediaries (**QIs**). We are seeking clarification regarding the interaction between the final Regulations entitled "Basis Reporting by Securities Brokers and Basis Determination for Stock" (the "**Regulations**") and the guidance provided in Notice 2011-34 (the "**Notice**") that provides for foreign financial institutions (**FFIs**) that are non-U.S. payors to be excluded from the cost basis reporting requirements.

### **Basis Reporting Requirements—Regulations**

Under the Regulations, a non-U.S. payor that is required to report proceeds on Form

1099-B will be subject to the cost basis reporting requirements when sales are effected at an office inside the U.S. Treas. Reg. §1.6045-1(g)(iii)(B)(3) sets out the rules for when a sale is considered to be effected at an office inside the U.S. These conditions include situations where:

1. the customer has opened an account with a U.S. office of the broker,
2. the customer has transmitted instructions concerning sales to the foreign office of the broker from within the U.S. by mail, telephone, electronic transmission or otherwise (unless the transmissions from the U.S. have taken place in isolated and infrequent circumstances),
3. the gross proceeds of the sale are paid to the customer by a transfer of funds into an account (other than an international account as defined in §1.6049-5(E)(4)) maintained by the customer in the U.S. or mailed to the customer at an address in the U.S.,
4. the confirmation of the sale is mailed to a customer at an address in the U.S., or
5. an office of the same broker within the U.S. negotiates the sale with the customer or receives instructions with respect to the sale from the customer.

The Canadian QI community has a number of account holders for whom payment will be considered to be effected at an office inside the U.S. primarily because of conditions #2 and/or #4 above. The Regulations will require cost basis reporting for these types of account holders.

In addition to the above noted requirements, the following comments included with the Regulations recognize that there should be coordination between the basis reporting requirements for non-U.S. payors and the reporting requirements under FATCA.

*“The Treasury Department and the IRS intend to issue future guidance coordinating the reporting requirements under section 6045 with the reporting requirements under section 1471.”*

Accordingly, it is our view that Treasury and the IRS left open the possibility of completely eliminating any cost basis reporting requirements once they considered the reporting requirements they would promulgate pursuant to section 1471.

### **Form 1099-B Reporting Requirements—QI Agreement**

Section 8.04 of the QI Agreement sets out a QI’s Form 1099-B reporting responsibilities for a “reportable payment” other than a “reportable amount”. Section 2.44 defines “reportable payment” as it applies to both U.S. and non-U.S. payors. In very general terms, proceeds of disposition realized on the sale of securities are included in the definition of “reportable payment” for a non-U.S. payor as follows:

- Proceeds from the disposition of U.S. securities are reportable payments if sales are effected in the U.S. within the meaning of Treas. Reg. §1.6045-1(a).
- Proceeds from the disposition of non-U.S. securities are reportable payments if payment is made in the U.S. within the meaning of Treas. Reg. §1.6049-5(e).

On this basis, Form 1099-B reporting of proceeds by a QI that is a non-U.S. payor is generally only required for U.S. non-exempt recipients residing in the U.S. Under the Regulations, for U.S. securities, once a sale is effected at an office inside the U.S., both proceeds and basis reporting are now required. Since the test is different for non-U.S. securities (payment made in the U.S.), it appears possible to have some accounts where a sale is effected in the U.S., but the payment is not made in the U.S. In such cases, we believe that since there wouldn't be any 1099-B reporting required under the QI Agreement for such non-U.S. securities, there also wouldn't be any cost basis reporting required.

#### **Basis Reporting Requirements—Notice 2011-34**

Section IV.C of the Notice states:

*“Treasury and the IRS intend to issue guidance providing that FFIs that are not U.S. payors (as defined in §1.6049-5(c)(5)) and that report the information required under section 1471(c)(1)(D) with respect to a U.S. account will not be required to report tax basis information required under section 6045(g) with respect to the account.”*

This section indicates that an FFI that is a non-U.S. payor and that enters into an FFI Agreement with the IRS and performs the required reporting under the FFI Agreement will not be required to perform cost basis reporting. The Notice sets out the details of the annual reporting for a U.S. account as required under section 1471(c)(1)(D) which will include the name, address, TIN, year-end account balances, gross income (interest, dividends and other income) paid or credited to the account, as well as gross proceeds paid or credited to the account with respect to which the FFI acted as a custodian, broker, nominee or otherwise as an agent for the account holder.

Based on the information in the Notice, FFIs that are non-U.S. payors that enter into an FFI Agreement with the IRS will not be required to report cost basis information. Since all QIs will be required to enter into an FFI Agreement, it appears that QIs that are non-U.S. payors and that perform the required reporting should be exempt from cost basis reporting.

## **The Inconsistency**

Given the proximity of Canada to the U.S., and the requirement that reporting occur for accounts where payment is effected at an office inside the U.S., the Canadian QI community has a number of account holders for whom cost basis reporting will be required under the Regulations. However, the Notice appears to provide for a complete exemption from cost basis reporting.

While the Notice appears to provide for a complete exemption, Canadian QIs are concerned that it is only a statement of intent, and that ultimately, the scope of the exemption may be more narrow than that necessary to provide for a complete exemption from cost basis reporting. When the Regulations were released, a general statement was made that non-U.S. payor QIs were exempt from cost basis reporting. However, a closer reading of the Regulations revealed a narrow exception to this rule that resulted in Canadian QIs being unable to make use of the exemption.

Since the Notice does not explicitly state an intention by Treasury to overrule the Regulations, our Canadian QI members are concerned that the possibility of a Participating FFI effecting sales in the U.S. was not contemplated. The concern is that the statement in the Notice regarding a forthcoming cost basis reporting exclusion was merely intended to advise FFIs that no new cost basis reporting requirements would be created by the 1471 regulations. Accordingly, our members are concerned that future 1471 regulations may be drafted in such a way that Canadian QIs would still need to comply with the Regulations and perform cost basis reporting when a sale is effected in the U.S.

## **The Urgency**

Although the number of account holders of Canadian QIs for whom basis reporting would be required under these rules will be significantly less than 1% of the total number of accounts that are subject to the QI Agreement, it is sufficiently high enough to make a manual process unworkable. Accordingly, the costs and resources associated with developing, implementing and maintaining the capability and capacity to comply with the cost basis reporting requirements are significant.

Canadian QIs are generally of the view that the uncertainty regarding the scope of the exemption provided for in the Notice leaves them no option but to continue to devote resources and funding to implement changes that may ultimately prove to be unnecessary. As you are aware, complying with FATCA will result in the QI community continuing to experience a scarcity of both resources and funding over the next several years.

***Accordingly, the Canadian QI community would welcome an immediate and clear statement from Treasury and the IRS that the FATCA regulations will ultimately completely exempt QIs that are non-U.S. payors from the cost basis reporting requirements and that such exemption will apply retroactively to January 1, 2011 (as basis reporting is applicable to certain securities purchased on or after January 1, 2011).***

We would greatly appreciate the opportunity to discuss this in more detail as soon as possible. Please contact me directly if you would like to arrange such a discussion, or if you have any questions.

Sincerely,



## Appendix “B”

Excerpt from the Office of the Privacy Commissioner (Canada). Full version is available at: [http://www.priv.gc.ca/fs-fi/02\\_05\\_d\\_02\\_e.cfm](http://www.priv.gc.ca/fs-fi/02_05_d_02_e.cfm)

### What is the Social Insurance Number (SIN)?

The Social Insurance Number (SIN) was created in 1964 to serve as a client account number in the administration of the Canada Pension Plan and Canada's varied employment insurance programs. In 1967, what is now Canada Revenue Agency (CRA) started using the SIN for tax reporting purposes.

### Who can ask for my SIN?

Your SIN is a confidential number that is restricted to income reporting purposes. There are a *select and limited number* of federal government departments and programs specifically authorized to collect the SIN. See list below.

The authority to collect and use the SIN is tied to a specific legislated purpose, *not* necessarily to a particular body. For example, an employer can collect an employee's SIN to provide them with Records of Employment and T-4 slips for income tax purposes, as can provincial or municipal agencies to report financial assistance payments for income tax purposes.

Institutions from which you earn interest or income, such as banks, credit unions and trust companies, must also ask for your SIN.

### How am I protected in the private sector?

The *Personal Information Protection and Electronic Documents Act* (PIPEDA) sets out ground rules for how private sector organizations may collect, use or disclose personal information in the course of commercial activities.

Since January 1, 2001, the Act applied to personal information about customers or employees that is collected, used or disclosed by the federally-regulated sector in the course of commercial activities. It also applies to information that is sold across provincial and territorial boundaries. As of January 1, 2004, the Act covers the collection, use and disclosure of personal information in the course of any commercial activity within a province, including provincially-regulated organizations, except in provinces that have enacted legislation that is deemed to be substantially similar to the federal law.

Under the new law, organizations like banks, telecommunications companies and airlines cannot require you to consent to the collection, use or disclosure of your personal information unless it is required for a specific and legitimate purpose.

This means that unless an organization can demonstrate that your SIN is required by law, or that no alternative identifier would suffice to complete the transaction, you cannot be denied a product or service on the grounds of your refusal to provide your SIN.

If you disagree with a request for your SIN made by an organization that is subject to the PIPEDA, you can complain to the Privacy Commissioner of Canada, who will investigate the complaint.

**Legislated uses of the SIN (or legislation that regulates its use) include:**

- Canada Pension Plan, Old Age Security and Employment Insurance contributions or claims (the original purposes for the SIN);
- Income Tax identification;
- banks, trust companies, caisse populaires and stock brokers when they sell you financial products (GICs or Canada Savings Bonds) or services (bank accounts) that generate interest. They declare your interest to Canada Revenue Agency (CRA) for income tax purposes;
- various Veterans Affairs benefit programs;
- Canada Student Loans or Canada Student Financial Assistance;
- Canada Education Savings Grants;
- Gasoline and Aviation Gasoline Excise Tax Applications;
- Canadian Wheat Board Act;
- Labour Adjustment Benefits Act;
- Tax Rebate Discounting Regulations;
- Race Track Supervision Regulations;
- Garnishment Regulations (Family Orders and Agreements Enforcement Assistance Act);
- Canada Elections Act;
- Canadian Labour Standards Regulations (Canada Labour Code);
- Farm Income Protection.

**Programs Authorized to use the SIN:**

- Immigration Adjustment Assistance Program;
- Income and Health Care Programs;
- Income Tax Appeals and Adverse Decisions;
- Labour Adjustment Review Board;
- National Dose Registry for Occupational Exposures to Radiation;
- Rural and Native Housing Program;
- Social Assistance and Economic Development Program

## APPENDIX “C”

### ***Classes of persons posing a low risk of tax evasion under Section 1471(f)(4) – retirement plans/other foreign entities***

Treasury and the IRS intend to issue guidance providing that certain foreign retirement plans pose a low risk of tax evasion for Chapter 4 purposes, and therefore payments beneficially owned by such retirement plans will be exempt from withholding under section 1471(a). Section II.E of the Notice also requests comments on the treatment of other foreign entities, including foreign charitable organizations.

The IIAC is pleased to see that Treasury and the IRS have taken into account the low risk associated with foreign retirement plans; however, the narrowing of the scope of the exemption by requiring an exempt retirement plan to be “sponsored by a foreign employer” will exclude registered personal retirement plans in Canada from the exemption when they in fact pose very low risks of tax evasion.

In Canada, the *Income Tax Act (Canada)* (the ITA) permits Canadian taxpayers to open accounts with financial institutions that are registered with and/or monitored by the Canada Revenue Agency (CRA) and are designed to provide tax advantages for individuals to increase personal savings generally (Tax Free Savings Accounts or TFSAs), for retirement (Registered Retirement Savings Plans or RRSPs and Registered Retirement Income Funds or RRIFFs), for education (Registered Education Savings Plans or RESPs) or for disabled individuals (Registered Disability Savings Plans or RDSPs). These arrangements are subject to terms and conditions set out in the ITA that are designed to limit the preferential tax treatment provided. In these plans, contributions to the plan might be tax deductible, or income and gains earned within the plan might be tax-exempt or tax-deferred until withdrawn. Under the ITA, these types of tax-assisted savings plans are only generally available to Canadian residents, must be registered with the CRA, and information such as contributions and withdrawals from the plans must be reported to the CRA by the plan administrator. Contributions to the plans are generally limited<sup>1</sup>, and excess contributions are subject to penalties.

***Given the regulatory restrictions attached to these accounts and the degree of the monitoring by the CRA to which they are subject, the IIAC recommends that they also be excluded from either the definition of FFI or from the definition of U.S. account on the basis that they present a low risk of being used by U.S. persons for tax evasion.***

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<sup>1</sup> Contributions to RRSP accounts are limited to the lower of \$22,000 or 18% of the taxpayer’s earned income for the previous year. Contributions to TFSA accounts are limited to \$5000 per year. RESP accounts are subject to a maximum \$50,000 lifetime limit with no annual limits. RDSP accounts are similarly subject to a maximum \$200,000 lifetime limit, with no annual limit.

Alternatively, Treasury and the IRS might consider exempting these registered retirement plans and other foreign entities (such as charitable organizations) because of their status as entities exempt from withholding under Article XXI of the Canada-U.S. Income Tax Treaty (the **Treaty**).

The Treaty includes provisions effectively allowing mutual recognition of certain tax-exempt entities. Under Article XXI, income of religious, scientific, literary, educational or charitable organizations exempt from tax in Canada is exempt from U.S. tax provided that such income is not from carrying on a trade or business. Article XXI similarly exempts from U.S. tax dividend and interest income derived by a trust, company, organization or other arrangement that is generally exempt from tax in Canada and that is operated exclusively to administer to provide pension, retirement or employment benefits. It seems appropriate that accounts of registered pension plans, RRSPs, RRIFs, RESPs, RDSPs and non-profit, educational, charitable and religious institutions that are exempt from tax in Canada and the U.S. under the Treaty should be excluded from the reporting and withholding requirements under sections 1471 and 1472.

***As such, the IIAC recommends the exclusion from the definition of FFI and/or U.S. accounts all Canadian entities or accounts that are covered by Article XXI of the Treaty.***

However, it may also be efficient for Treasury and the IRS to contemplate drafting regulations that would exclude from the definitions of FFI and/or U.S. account, all entities that are similarly covered under the tax treaties that have been negotiated between the U.S. and other countries. This would provide a global approach to the exclusion, as it could be applied to every country that has a tax treaty with the U.S.