INVESTMENT
INDUSTRY ASSOCIATION
OF CANADA

Letter from the President

Caught in the Vice: Dealer Efforts to Extricate from Draconian U.S. Tax Reporting Requirements

The Problem

The Association has worked closely with the Internal Revenue Service (IRS) and the U.S. Department of the Treasury (Treasury) in recent years to develop reasonable reporting and audit requirements for IRS approved Qualified Intermediaries (QIs). Non-U.S. investment dealers that qualify and have entered into QI Agreements with the IRS assume documentation and withholding responsibilities in exchange for simplified information reporting for their account holders. This preferred status is given to Canadian and other foreign dealers that meet the defined audit and tax reporting requirements set by the IRS.

In the past year, these QI reporting requirements have been overtaken by a more vigorous and overarching U.S. policy initiative to address perceived tax evasion by U.S. investors. In the wake of the investigation and settlement with UBS, U.S. legislators have pushed to identify U.S. persons suspected of evading U.S. tax reporting requirements in their dealings with foreign financial institutions.

In early 2009, the Obama administration introduced proposals referred to as the *Green Book*, recommending sweeping tax reporting obligations that would apply to both QI and non-QI foreign financial institutions. While well intentioned, the *Green Book* proposals would have translated into unreasonable and onerous reporting requirements for foreign financial institutions holding accounts for U.S. persons. These foreign institutions include Canadian investment dealers already subject to QI requirements as well as other foreign banks, dealers, insurance companies and other institutions offering financial services to U.S. investors.

The IIAC worked independently and through international associations such as the Institute of International Bankers (IIB), to explain the significant costs associated with compliance, the contradictions relative to international law and tax treaties and the complications for foreign institutions subject to investor privacy laws. Further, the IIAC argued the *Green Book* proposals would disadvantage U.S. investors and damage U.S. capital markets as foreign institutions are discouraged from opening accounts with U.S. persons and, as well, the onerous reporting obligations act as a disincentive for QI status and thereby discourages investment in U.S. dividend-paying stocks.

A modified version of the *Green Book* proposals was introduced in the U.S. Congress last November as the *Foreign Account Tax Compliance Act of 2009*. The Act will require all foreign financial institutions to enter into agreements with the IRS to disclose individual account information about each of its clients that are U.S. persons (regardless of whether they are receiving U.S. source income), or face a full 30% withholding rate for all payments to all accountholders (regardless of whether they are U.S. persons). These requirements will supercede existing tax treaty agreements, local privacy legislation, and QI agreements.

What the IIAC is doing?

Through its QI Committee, the IIAC made submissions to Congress, Treasury and the IRS arguing the onerous and far-reaching nature of the proposed reporting obligations, the extra-territoriality of the proposed legislation and disregard for international tax protocols to address tax evasion problems through bi-lateral and multi-lateral negotiations. Representatives of the IIAC Committee also met with legislators on Capitol Hill as part of delegations organized by the IIB. The pending legislation was modified somewhat in response to international lobbying efforts and, as part of the *Tax Extenders Act*, was passed by the House of Representatives last month. It is anticipated that the bill will pass the Senate early in the New Year, and that Treasury will draft regulations to implement the requirements throughout 2010.

Our lobbying efforts, in conjunction with the international financial community, have been successful in several respects. First, we have delayed the reporting requirements under the new legislation for an additional two year period to give sufficient time to argue for alleviating the reporting burden under the legislation. Second, the revised legislation gives the Treasury increased discretion to impose certain "carveouts" from the legislation. The IIAC Committee will argue for an exemption for QI-designated dealers already subject to significant IRS reporting and audit obligations. Third, the *de minimis* account size for reporting purposes was raised from $10,000 to $50,000.

We have also raised this matter with the Federal Department of Finance to encourage direct engagement with Treasury to meet tax evasion concerns through formal bi-lateral negotiations that build on the existing framework.

The coming year will be an active one for the Canadian dealer community as we continue efforts to extricate the industry from onerous U.S. tax reporting regulations. Our objective is to achieve an efficient compromise in terms of imposing reasonable tax reporting obligations to meet tax evasion concerns without jeopardizing active cross-border trading and investing in marketable securities.

Yours sincerely,

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President & CEO, IIAC

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