IIACACCVM
INVESTMENT INDUSTRY ASSOCIATION OF CANADA
ASSOCIATION CANADIENNE DU COMMERCE DES VALEURS MOBILIÈRES

LETTER FROM THE PRESIDENT

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Global Tax Reporting: The IIAC's Efforts to Help Member Firms Navigate a Changing Landscape

HIGHLIGHTS:

The IIAC U.S. Tax Committee and its various working groups have been actively involved in the past six years as FATCA has been rolled out.

The Committee worked with the CRA and IIROC to clarify the obligations of both introducing and carrying brokers to ensure that all account documentation, reporting and withholding requirements of FATCA and QI (Qualified Intermediary) aligned with responsibilities under existing carrying arrangements.

The IIAC has produced tools for understanding the inter-connected FATCA, QI and OECD Common Reporting Standard (CRS) requirements, and will build on these efforts.

The IIAC has been fully engaged with U.S. authorities to discuss the operational challenges in implementing rules related to U.S. withholding requirements on payments derived from underlying U.S. securities.

The IIAC OECD working group will solicit input from Member Firms on the global tax reporting requirements under the newly proposed Part XIX of Canada's *Income Tax Act*.

In 2008, the U.S. Congress became increasingly alarmed about tax avoidance and evasion—money routed through foreign tax havens. A U.S. Senate report claimed that the annual lost tax revenue from offshore banking could total as much as $100 billion.

At the same time, the U.S. Federal Bureau of Investigation engaged in a formal investigation of a multi-billion-dollar tax evasion case involving a Swiss bank. The Internal Revenue Service (IRS) reached a landmark settlement agreement with the Swiss bank to provide tax records of U.S. citizens to the IRS to crack down on tax evasion, banking and investment accounts that had hitherto been kept confidential. The U.S. authorities leveraged the threat of penalties, including the loss of U.S. banking license. In June 2010, Swiss law-makers approved a final deal to hand over data and account details of U.S. clients suspected of tax evasion. A tax treaty between Switzerland and Washington established the legal basis for this course of action.

During this period, the Foreign Account Tax Compliance Act (FATCA) was introduced in Congress in 2009, and enacted in 2010 as part of the Hiring Incentives to Restore Employment (HIRE) Act. FATCA requires foreign financial institutions to report certain information about financial accounts held by U.S. taxpayers, or by foreign entities in which U.S. taxpayers hold a substantial ownership interest either directly to the IRS, or by negotiated international agreement, to their local tax authority. This information is then provided to the IRS. Foreign financial institutions that fail to comply with the FATCA requirements face significant U.S. withholding taxes on all payments they receive from U.S. sources, and, potentially, penalties applied under local tax law.

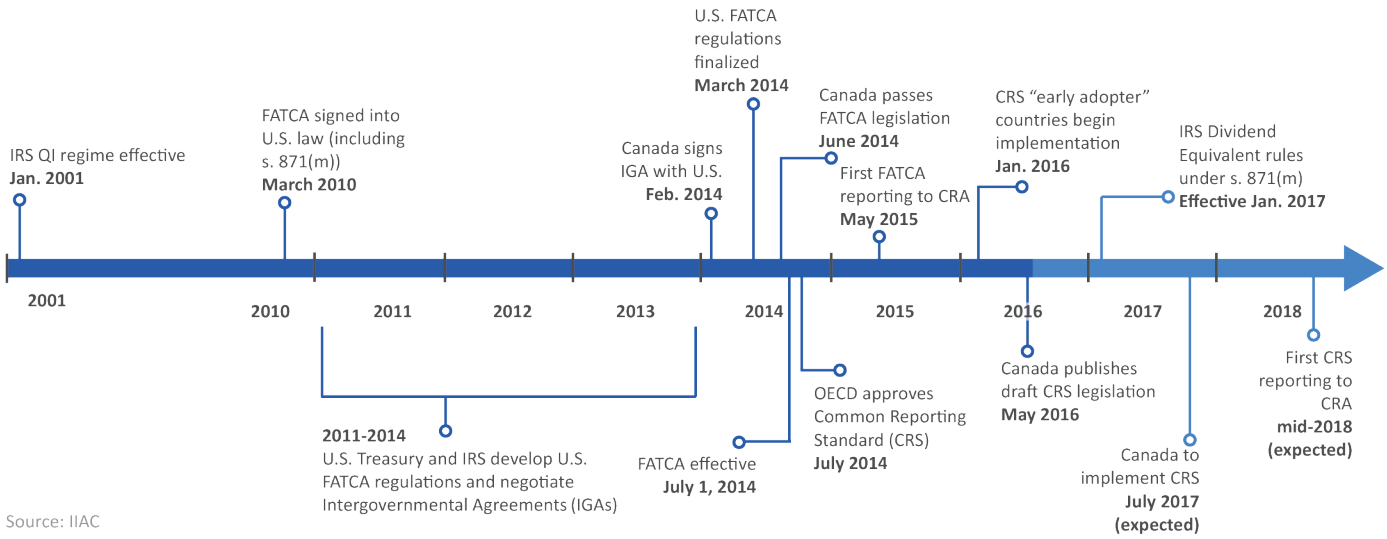
The U.S. FATCA regulations, and the intergovernmental agreements (IGAs) struck in many countries, including Canada, to implement the requirements, were developed in consultation with many foreign financial institutions and governments. Much of the consultations focused on practical and cost-effective compliance requirements, exemptions or "carve-outs" from the reporting requirements, and the time required to put in place needed technology and reporting procedures. The carve-outs, for the most part, included registered tax-assisted financial accounts for retirement and other purposes (such as RRSPs, RRIFs, RESPs, RDSPs and TFSAs), and instruments with limited scope and relevance as tax-evasion vehicles.

The IIAC Value Proposition

The IIAC U.S. Tax Committee and its various working groups have been actively involved in the past six years as FATCA has been rolled out. The Committee and working groups provided a forum for IIAC Member firms to share relevant information as the proposed requirements evolved, and develop an acceptable industry position on proposed legislation. The Committee advocated for cost-effective reporting to meet the policy objective of curbing tax evasion, and made the case for sensible exemptions from the reporting rules, and obtained needed delays to ensure full compliance with the legislation. A joint Canadian financial industry group, including the IIAC, urged both U.S. and Canadian officials to enter into an IGA which gave the Canada Revenue Agency (CRA) the responsibility of collecting and transferring the required tax information in an efficient and secure manner to the IRS.

The industry was successful in obtaining the time necessary for the implementation of the FATCA reporting obligations, including a two-year phased-in approach for identifying and reporting accounts, and a two-year "soft-landing" period in 2014 and 2015 which allowed financial institutions to use their best efforts to implement FATCA without fear of penalty, as both the industry and the CRA continue to resolve various ongoing implementation challenges.

Global Exchange of Tax Information: The Evolution



Source: IIAC

Since the official FATCA effective date of July 1, 2014, the IIAC U.S. Tax Committee and working groups have focused efforts on a number of related initiatives of particular importance to IIAC members, including:

1. Tools for understanding the interconnected FATCA, QI and OECD Common Reporting Standard (CRS) requirements

Canadian dealers that are "Qualified Intermediaries" (QIs) faced unique challenges when implementing FATCA. These QIs were already following complex IRS rules to document account holders as either U.S. or non-U.S. persons, and if necessary, apply the required U.S. withholding tax under the applicable tax treaty and provide the necessary reporting to the IRS and clients. The IIAC U.S. Tax Committee engaged a recognized global tax accounting firm to assist in the development of a tool to help Member firms understand the complex requirements for reporting and withholding on account holders who do not provide the necessary documentation to determine their status (known as the "presumption rules").

This tool identifies for each type of payment and type of account holder the process for identifying the account holder's status under both regimes, the applicable withholding rate, and the potential reporting to both CRA (for FATCA) and the IRS (for QI). This work has been invaluable to IIAC members in developing an industry-standardized approach to the application of these rules.

Now that the tax reporting requirements under the OECD CRS (Common Reporting Standard), have been proposed for inclusion in the *Income Tax Act*, effective July 2017 (see above), the IIAC will be working toward building another layer onto this tool to determine how the global tax reporting requirements will interact with the existing FATCA and QI regimes.

2. Clarifying Tax Reporting Obligations of IIROC-Registered Brokers

The IIAC U.S. Tax Committee worked with the CRA and the Investment Industry Regulatory Organization of Canada (IIROC) to clarify the obligations of both introducing and carrying brokers to ensure that all account documentation, reporting and withholding requirements of FATCA and QI aligned with responsibilities under existing carrying arrangements. Generally, under the CRA FATCA guidance and industry standard agreements, the introducing broker remains responsible for the accurate identification of their client accounts as reportable, and for passing this information to its carrying broker, who will undertake the reporting function on behalf of the introducing broker. The IIAC is working with the CRA to obtain similar clarification of responsibilities for IIROC carrying brokers reporting relevant tax information to the CRA on behalf of non-IIROC registered portfolio managers. The IIAC will also be recommending similar guidance be adopted with respect to global tax reporting obligations under the CRS.

3. U.S. withholding requirements on payments derived from underlying U.S. securities (IRS Section 871(m) and Section 305(c))

Under certain sections of the U.S. Internal Revenue Code, payments made under certain instruments derived from an underlying U.S. security (section 871(m)) or that are deemed to occur because of corporate action or conversion rate adjustment with respect to a U.S. security (section 305(c)) are considered to be U.S. source income by the IRS, and as such, subject to the U.S. tax withholding and reporting requirements. These rules impact a broad group of investment products including swaps, options, forwards, futures, convertible debt instruments and other similar contractual arrangements, many of which had hitherto been exempt from U.S. tax withholding and reporting.

The IIAC has been fully engaged with U.S. authorities to discuss the operational challenges in implementing these rules, such as their impact on listed derivatives. The Committee has also requested sufficient lead time as many of these newly proposed regulations require significant back-office operational builds to link the capital markets and tax withholding/reporting systems.

4. Proposed Global Tax Reporting Requirements Under CRS

The global tax reporting requirements under the newly proposed Part XIX of Canada's *Income Tax Act* are now out for public comment. The IIAC's OECD CRS Working Group will pull together views and opinion from IIAC Member firms on specific recommendations to ensure cost-effective and practical rules for compliance.

The IIAC has also developed an FAQ for clients of IIAC Member firms in connection with the CRS tax reporting requirements. The FAQ will describe the purpose of the tax reporting requirements, how clients may be affected by the requirements, describe the CRA's role in reporting to other jurisdictions and other commonly asked questions. For more detailed information about any of these initiatives, the IIAC U.S. Tax Committee, OECD CRS Working Group, or to obtain a copy of the CRS FAQ, please contact Andrea Taylor (ataylor@iiac.ca).

Yours sincerely,

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