



THE INVESTMENT FUNDS INSTITUTE OF CANADA
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

Joanne De Laurentiis
PRESIDENT & CEO

BY EMAIL

March 8, 2011

Ms. Jane Pearse
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Dear Ms. Pearse

Re: Foreign Account Tax Compliance Act – IFIC Discussions with U.S. Treasury and IRS Officials

I am writing to advise you about our meeting with officials of the United States Treasury and Internal Revenue Service ("IRS") concerning the application to Canadian mutual funds of the "Foreign Account Tax Compliance Act" ("FATCA") provisions in the US Internal Revenue Code.

Under FATCA, a "foreign financial institution" such as a Canadian mutual fund is required to enter into an agreement with the IRS to perform certain functions relating to the identification and reporting of "US accounts" (i.e., investors that are US citizens or other US persons) and withholding from amounts distributed to "recalcitrant accounts", failing which the fund will be subject to a 30% US withholding tax on certain income and proceeds from disposition.

At the meeting, we indicated that our industry is sympathetic to the policy objectives sought to be achieved by FATCA, being the reduction of tax evasion by US persons, but submitted that Canadian mutual funds pose little risk of tax evasion by US persons because Canada imposes a 25% withholding tax on certain distributions by Canadian mutual funds and, pursuant to automatic exchange of information arrangements between the CRA and IRS under the Canada-US Income Tax Convention, the CRA provides information to the IRS about distributions made to persons with US addresses. While such information is not sorted by US taxpayer identification number (or TIN), we believe that where amounts are material, the IRS can take the necessary steps to associate the information provided to the relevant taxpayer. It was noted at our meeting that there is no reporting of dispositions of Canadian mutual fund securities (i.e., as far as we are aware, T5008 information is not exchanged) for accounts that are not registered plans.

We also noted that the requirements to be satisfied under FATCA are onerous and will require changes to account opening procedures.

Ms. Jane Pearse

Re: Foreign Account Tax Compliance Act – IFIC Discussions with U.S. Treasury and IRS Officials

Taking into account the foregoing, at our meeting we presented two alternative treatments for widely held Canadian mutual funds. Under the first alternative, if certain conditions were met, including that not more than 10% of investors were resident outside Canada and the United States, employing the "address" rule contemplated by the CRA in Information Circular 76-12R6, a fund would not have to enter into an agreement with the IRS. If these conditions were not met, our second alternative was that the diligence process to determine US account status be modified. We also submitted that it should not be necessary to determine if the beneficiary, annuitant or holder, as applicable, of Canadian registered plans such as RPPs, RRSPs, RRIFs, DPSPs, RDSPs, RESPs and TFSAs is a US person. A copy of our presentation is included for your reference.

The US officials at the meeting were somewhat sympathetic to our position, particularly in relation to registered plans, but non-committal. They asked that we provide them with some additional information and we have done so. A copy of our response is enclosed for your reference.

We would like to arrange a further call with you to continue our discussions.

Yours very truly,

A handwritten signature in blue ink, consisting of a large, stylized initial 'C' followed by a horizontal line extending to the right.

CC: Francois Beaudry, Office of the Honourable James Flaherty (Francois.Beaudry@fin.gc.ca)

Attachment



The Investment Funds Institute of Canada

Presentation to the International Tax Counsel

**Alternative FATCA Compliance Approaches for
Canadian Mutual Funds**

Monday, January 10, 2011

IFIC Representatives

- Barbara Amsden, The Investment Funds Institute of Canada
- Debbie Pearl-Weinberg, General Tax Counsel, Canadian Imperial Bank of Commerce, and Chair, IFIC Tax Committee
- David Jerome, Director of Tax Operations, RBC Dexia Investors Services Trust
- Hugh Chasmar, Partner, Deloitte
- Paul Epstein, Partner, Deloitte
- Nigel Johnston, Partner, McCarthy Tetrault LLP
- Ron Wilson, Partner, Davies Ward Phillips & Vineberg, LLP

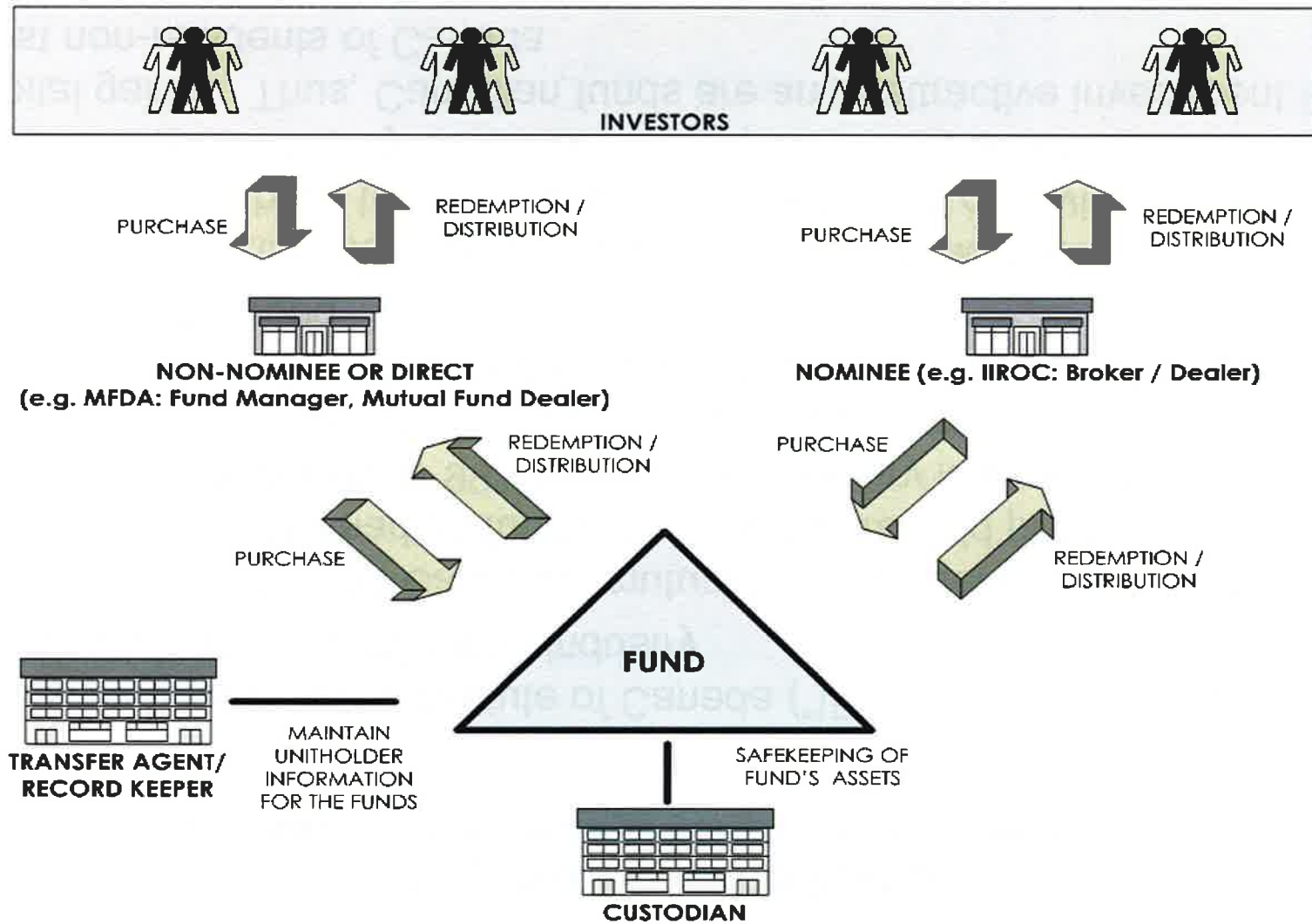


Key Background Facts

- The Investment Funds Institute of Canada ("IFIC") is the trade association of Canada's investment funds industry
- Prospectus distributed Canadian mutual funds as defined under Canadian securities laws ("Canadian funds" or "funds") are sold primarily to Canadian investors (approximately 99%). Thus, our industry is similar to the US mutual fund industry where US funds are sold primarily to US investors and is quite different from the fund industry in some of the specialized financial centres of the world
- This occurs partly because Canadian non-resident withholding tax at the rate of 25% (subject to treaty reduction) is imposed on dividends and other income distributions by Canadian funds (and on some distributions of capital gains). Thus, Canadian funds are an unattractive investment for most non-residents of Canada
- This presentation comments on and refines some of the proposals set out in our submission of November 1, 2010. We are pleased to be able to discuss these proposals with you and to respond to any questions or concerns you may have



Canadian Fund Industry Structure



Alternative FATCA Compliance Approaches for Canadian Mutual Funds

- Low risk fund approach - Section 1471(f)
- Not necessary approach - Section 1471(b)(2)(B)
- Compliance agreement approach - Section 1471(b)(1)
- No United States accounts approach - Section 1471(b)(2)(A)
- Additional points or issues



Overview on Proposed Approaches

- A Canadian fund is proposed as a low risk fund if fund investors are of a type in respect of which there is no risk or a low risk of US tax evasion
- A form of compliance agreement is proposed for Canadian funds which only requires the fund to obtain and report information for investors of a type in respect of which there is a greater than low risk of US tax evasion
- Our two approaches are viable because of the existing automatic exchange of information arrangements between our two countries



Low Risk Fund Approach - Section 1471(f)

- The fund is not fiscally transparent (i.e., it is a taxpayer and files tax returns in Canada, although it may be able to avoid Canadian tax by making distributions in a manner similar to a RIC)
- The fund is a resident of Canada for purposes of the Canada-US tax treaty and a qualifying person for purposes of the LOB provision in such treaty
- The fund has at least 100 investors (subject to a transition rule on start-up)
- More than 90%, or other prescribed percentage, of the investors in the fund by value
 - are treated by the fund as tax residents of Canada in accordance with fund and CRA guidelines,
 - hold their investments in the fund at foreign financial institutions which have entered into a FATCA compliance agreement,
 - hold their investments in a Canadian registered plan, or
 - have an address in the United States
- Investors who are tax residents of Canada are already subject to Canadian income tax, which tax is generally creditable against any US tax otherwise payable

Low Risk Fund Approach cont'd - Section 1471(f)

- Foreign financial institutions which have entered into a FATCA compliance agreement are already subject to FATCA reporting and withholding
- Investments in Canadian registered plans are either held for retirement purposes or to comply with statutorily prescribed social purposes (in which case they are generally modest in amount) - see also Appendix A
- Information on US address investors is already automatically reported by the CRA to the IRS under the Exchange of Information provision in the Canada-US tax treaty. Thus, further reporting would arguably be "duplicative" for purposes of Section 1471(d)(1)(C) - see also Appendix B
- Each investor in the fund not described above owns securities of the fund with a value of
 - less than \$20,000, or
 - if more than \$20,000, when aggregated with all securities owned by the investor in other funds managed by the manager, less than the final *de minimus* amount for accounts at a single institution (currently proposed to be \$50,000)

Not Necessary Approach - Section 1471(b)(2)(B)

- We presume that the low risk fund approach outlined in the previous two slides might also qualify a fund as satisfying the requirements of the not necessary approach



Compliance Agreement Approach – Sections 1471(b)(1)(A) to (F)

- Proposed form and terms of agreement for Canadian resident mutual funds
- The agreement would be entered into by a fund manager on behalf of all funds specified in a schedule to the agreement
- (A) The agreement would except the fund from obtaining and reporting information for any investor who
 - is treated by the fund as a tax resident of Canada in accordance with fund and CRA guidelines,
 - holds the investment at a foreign financial institution which has entered into a FATCA compliance agreement,
 - holds the investment in a Canadian registered plan, or
 - has an address in the United States
- As already noted, investors who are tax residents of Canada are already subject to Canadian income tax, which tax is generally creditable against any US tax otherwise payable
- As already noted, foreign financial institutions which have entered into a FATCA compliance agreement are already subject to FATCA reporting and withholding

Compliance Agreement Approach cont'd – Sections 1471(b)(1)(A) to (F)

- As already noted, investments in Canadian registered plans are either held for retirement purposes or to comply with statutorily prescribed social purposes (in which case they are generally modest in amount)
- As already noted, information on US address investors is already automatically reported by the CRA to the IRS under the Exchange of Information provision in the Canada-US tax treaty. Thus, further reporting would arguably be "duplicative" for purposes of Section 1471(d)(1)(C)
- (B) The agreement would require the fund to comply with verification and due diligence procedures as specified for reportable investors
- (C) The agreement would require the fund to comply with reporting procedures as specified for reportable investors
- (D) The agreement would provide for withholding on passthru payments to recalcitrant holders using an administrable asset based approach

Compliance Agreement Approach cont'd – Sections 1471(b)(1)(A) to (F)

- (E) The agreement would require the fund to comply with requests from the Secretary for additional information
- (F) The agreement would require the fund to comply with Section 1471(b)(1)(F)

No United States Accounts Approach - Section 1471(b)(2)(A)

- Likely not currently relevant to most widely held Canadian mutual funds
- However, these types of funds might be established in the future



Related Points and Issues

- Treating interests in Canadian funds as excepted from the definition of "financial account" on the basis that they are effectively "interests which are regularly traded on an established securities market"
- The reclaim process
- Drafting of definition of low risk fund and standard form compliance agreement
- Contact person for further discussions

Appendix A – Additional Information on Canadian Registered Accounts

- Canadian Registered Plans For Retirement Purposes
 - *Registered Pension Plan (RPP)* - A RPP is an employer sponsored group retirement plan. Employer and employee contributions are subject to statutory limits. Employee contributions must be sourced from employment income. Income earned within a RPP is not subject to tax. Pension payments received from a RPP are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada).
 - *Deferred Profit Sharing Plan (DPSP)* - A DPSP is another type of employer sponsored group retirement plan. Contributions to a DPSP are subject to statutory limits. Income earned within a DPSP is not subject to tax. Withdrawals from a DPSP are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada).
 - *Registered Retirement Savings Plan (RRSP)* - A RRSP is an individual retirement plan. Annual contributions are limited to \$22,450, subject to adjustment for inflation. Income earned within a RRSP is not subject to tax. Withdrawals from a RRSP are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada). Funds in a RRSP must be used to purchase an annuity or transferred to a RRIF before the end of the year when the beneficiary turns 71.
 - Note that the statutory contribution limits for RPPs, DPSPs, and RRSPs are integrated.
 - *Registered Retirement Income Fund (RRIF)* - The funds in a RRSP may be transferred to a RRIF. There is a minimum required annual withdrawal from a RRIF. Income earned within a RRIF is not subject to tax. Withdrawals from a RRIF are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada).



Appendix A cont'd – Additional Information on Canadian Registered Accounts

- *Tax-Free Savings Account (TFSA)* - The TFSA is a tax pre-paid savings plan. Annual contributions are limited to \$5,000 annually for Canadian residents, subject to adjustment for inflation. Non-residents are not permitted to contribute to a TFSA. Income earned within a TFSA is not subject to tax. Withdrawals from a TFSA may be made at any time and are not subject to tax.
- Canadian Registered Plans For Other Specified Social Purposes
 - *Registered Disability Savings Plan (RDSP)* - Designed to assist parents and others to save for the long-term financial security of a person with a severe disability. There is a lifetime contribution limit of \$200,000 for all the plans of the disabled person. There is no annual contribution limit. Amounts withdrawn in excess of contributions are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada).
 - *Registered Education Savings Plan (RESP)* - Designed to assist in saving for a child's post-secondary education. There is a lifetime contribution limit of \$50,000 for each child. There is no annual contribution limit. Amounts withdrawn in excess of contributions are subject to tax (including Canadian non-resident withholding tax if the recipient is a non-resident of Canada). Penalty taxes may apply if the earnings are not used for post-secondary education.



Appendix B – Exchange of Information Comments

- The following is from the Income Tax Treaties Reference Manual of the Canada Revenue Agency. It was obtained under *The Access to Information Act* (Canada):

"Automatic (or Routine) Exchange

Automatic exchanges of information about the systematic transmission of information concerning various categories of income (i.e., dividends, interest) to and from treaty partners.

Under the Canada-US Convention (Information to be provided by each party)

2. The competent authority of Canada shall forward to the Competent Authority of the US as soon as practicable after the close of each calendar year, the following information relating to such calendar year:

(a) The names and addresses of all persons whose addresses are within the US who derived from sources within Canada dividends, interest, rents, royalties, salaries, wages, pensions, or other fixed or determinable annual or periodical profits and income, showing the amount of such profits and income in the case of each addressee"





THE INVESTMENT FUNDS INSTITUTE OF CANADA
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA

February 17, 2011

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Dear Sirs:

Re: Foreign Account Tax Compliance Act January 10, 2011 Meeting: Further Information

Thank you for meeting with us on January 10, 2011 regarding our recent submission on particular aspects of the FATCA legislation. Please find attached further information that we undertook at the meeting to provide to you.

1. The legislation currently includes an exemption from due diligence for depository accounts with balances under \$50,000. In our submission, we requested an expansion of that exemption to include non-depository accounts such as mutual funds, and in evaluating our submission, you have asked for data confirming that such a change will impact a significant number of accounts. We attach the results of our member survey, responded to by members accounting for 72% of IFIC reported Assets under Management. The survey clearly demonstrates that this would apply to a meaningful number of accounts. (See *Annex A*).
2. You also had requested further details on account opening information collected, and the capability to electronically search this data. Please find attached details of our findings. (See *Annex B*). The following is a summary of our findings:
 - Currently the only information which is electronically searchable by a Canadian mutual fund manager for mutual fund accounts in Canada is the investor's name, address, social insurance number (and sometimes date of birth). Additional information obtained by the distributing dealer under the KYC rules is generally retained only in photocopy form and thus is not electronically searchable. In some cases, the additional information is retained as a PDF or other



similar electronic image. However, the vast majority of such electronic images are generated from scanning (as opposed to directly from a Word or other word processor document) and thus are also not generally electronically searchable.

- The only accounts which Canadian mutual fund managers can currently identify as United States Accounts (as defined in the FATCA legislation) are accounts of persons with a United States address.

3. Finally, you had indicated that any exemption granted from the definition of “United States account” for registered plans would not be country specific. We attach some draft language that you may consider in preparing non-country-centric language exempting certain registered plans from the definition of “United States account”. (See *Annex C*)

Please do not hesitate to contact us should you have any questions regarding the attached documents, or require further information.

We look forward to continuing these discussions with you.

Yours sincerely,



Debbie Pearl-Weinberg, Chair – Taxation Working Group/IFIC

Cc: Manal Corwin, U.S. Department of the Treasury - Office of International Tax Counsel
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Jane Pearce, Director, Financial Institutions Division, Department of Finance (Canada)
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Data Indicating the Percentage of Accounts with Balances Under \$50,000

Firm Number	Percentage of Accounts under \$50,000	Assets under Management December 2010 (\$Billion)
1	84%	
2	93%	
3	90%	
4	63%	
5	94%	
6	88%	
7	93%	
8	96%	
9	90%	
10	89%	
11	65%	
Asset-Weighted Percentage	86%	
Sample Total Assets under Management		456.1
IFIC Reported Total Assets under Management*		635.6
Sample as Percentage of IFIC Reported Assets		72%

*Assets reported by IFIC representing approximately 85% of total industry mutual fund assets under management.

Potentially Searchable Information for Canadian Mutual Fund Accounts

1. **Introduction** During our meeting with you on January 10, we undertook to provide you with precise details regarding the information collected in respect of mutual fund accounts in Canada, and the extent to which such information is electronically searchable by the mutual fund managers. The collection and retention practices depend upon two principal variables, namely, the category of registration of the information collector and the type of account of the client. Accordingly, these two variables are discussed below.
2. **Categories of Registration** There are two relevant registration categories:
 - (a) **Investment Fund Managers** A mutual fund manager is required to be registered as an investment fund manager or (IFM) by the provincial securities commission in which its head office is located. IFMs generally do not sell their mutual funds directly to the public, but rather sell them through mutual fund dealers or investment dealers ("Dealers"). The Dealers, in turn, engage registered representatives. Thus, the IFM is not responsible for collecting know-your-client ("KYC") information or identifying clients for the purposes of anti-money laundering ("AML") legislation.
 - (b) **Dealers** Dealers generally do not manage investment funds. Rather, they sell mutual funds to investors on behalf of IFMs. Thus, dealers (and their registered representatives) are responsible for collecting KYC information and identifying clients for AML purposes. Dealers and their representatives are registered with the provincial securities commissions in the provinces where they conduct business and have clients. In addition, they must belong to a self regulatory organization ("SRO"). Mutual fund dealers belong to and are regulated by the Mutual Fund Dealers Association of Canada ("MFDA"), while investment dealers belong to and are regulated by the Investment Industry Regulatory Organization of Canada ("IIROC").
3. **Anti-Money Laundering** The *Proceeds of Crime (Money Laundering) and Terrorist Financing Act* (Canada) sets out rules applicable to Dealers for identifying clients upon the opening of accounts.
4. **Recording Keeping Practices** The information which is collected and retained by an IFM in respect of a mutual fund account will be a subset of the information which is required to be obtained by the Dealer upon the opening of the account pursuant to the KYC rules. The information will vary depending on the type of mutual fund account as described below. As a general rule, documents are retained for at least seven years after an account has been closed.
5. **Types of Accounts** There are four types of mutual fund accounts administered by IFMs in Canada:

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- (a) **In-House Accounts** In-house accounts arise where the IFM also acts as the Dealer. These accounts are generally only for employees and their families and some institutional clients, and typically account for less than 1% of all IFM accounts.
 - (b) **Client Name Accounts** Client name accounts are opened by a Dealer, but are recorded in the client's name at the IFM. The Dealer collects all the KYC and identification information, and then places the trade with the IFM. The IFM issues all required tax receipts for these accounts to the client, based on the information provided by the client and the Dealer.
 - (c) **Nominee Accounts** Nominee accounts are opened by a Dealer and are recorded in the name of the Dealer (as the Nominee for the client). The Dealer is not only responsible for the collection of KYC and identification information, but also is responsible for recordkeeping. Thus, all instructions regarding payments are received from the Dealer, and all distributions are made to the Dealer.
 - (d) **Intermediary Accounts** Intermediary accounts are similar to nominee accounts, except that they are maintained at a trust company which administers retirement or pension accounts on behalf of clients. As with nominee accounts, all instructions regarding payments are received from the intermediary, and all distributions are made to the intermediary.

The majority of the mutual fund accounts in Canada are recorded in nominee or intermediary name, while most of the remainder are recorded in client name. The following three sections itemize the information which is typically collected and retained by the IFM for the four types of accounts described above.

6. **In-house Accounts** For in-house accounts, the IFM collects and retains the KYC and AML identification information. Thus, the following information is typically collected and retained by the IFM:

- (a) Name
- (b) Address
- (c) Date of birth
- (d) Social insurance number
- (e) Occupation
- (f) Net worth
- (g) Annual income

- (h) Investment knowledge, objectives, risk tolerance
- (i) Documents evidencing identification:
 - (i) photocopies of government issued documents (e.g., driver's license, passport, birth certificate), or
 - (ii) photocopies of credit check information and a cleared cheque for an account at a Canadian bank

7. **Client Name Accounts** For client name accounts, the following information is typically received and retained by the IFM:

- (a) Name
- (b) Address
- (c) Date of birth
- (d) Social insurance number

8. **Nominee and Intermediary Accounts** For nominee and intermediary accounts, the following information is typically received and retained by the IFM:

- (a) Name
- (b) Address
- (c) Social insurance number

9. **Electronic Searchability of Information** Currently the only information which is electronically searchable by an IFM for mutual fund accounts in Canada is the information retained for the purpose of administering the account. Moreover, the additional information obtained by the Dealer under the KYC rules is generally retained only in photocopy form and thus is not electronically searchable. In some cases, the additional information is retained as a PDF or other similar electronic image. However, the vast majority of such electronic images are generated from scanning (as opposed to directly from a Word or other word processor document) and thus are also not generally electronically searchable.

10. **Conclusion** Based on the above facts, the only accounts which Canadian mutual fund managers or IFMs can currently identify as United States Accounts (as defined in the FATCA legislation) are accounts of persons with a United States address. As noted in our submission of January 10, 2011, the Internal Revenue Service already receives information from the Canada Revenue Agency on such persons under the automatic exchange of information arrangements entered into between the two organizations pursuant to Article XXVII of the Canada-United States Tax Convention.

Proposed Draft Regulations in Respect of Registered Plans

Pursuant to the authority provided by paragraph 1471(f)(4), the following persons are identified by the Secretary and are prescribed as posing a low risk of tax evasion and thus subsection 1471(a) does not apply to such persons:

- a. A trust, plan or other arrangement (referred to herein as “the plan”) that is accepted for registration as and qualifies as a retirement plan under the tax law of the country in which it is established and which has all of the following attributes under such tax law:
 - i. The assets of the plan are to be held for the purpose of providing retirement income to the individual who established the plan (the “contributor”) or to a spouse or common-law partner of the contributor;
 - ii. Where contributions to the plan are deductible in computing the income of the contributor, withdrawals from the plan are required to be included in the income of the recipient thereof;
 - iii. Income and gains realized in respect of assets retained within the plan are not subject to tax until such income or gains are withdrawn from the plan, at which time such amounts would be included in the income of the recipient;
 - iv. A contributor must have income from employment or income from carrying on business in order to be permitted to make tax-deductible contributions to the plan. All other permitted contributions to the plan must be from another retirement plan of the individual or of a spouse, common-law partner of the individual, or of a parent or grandparent of the individual where the individual is financially dependent on the parent or grandparent;
 - v. The amount of the annual or cumulative life-time tax-deductible contributions to the plan a limited to such amount as the government of the particular country considers to be sufficient to provide a retirement income comparable to that which would be provided by a registered employer sponsored defined benefit pension plan and will be reduced on a formula basis for a particular individual that is a member of such a pension plan; and,
 - vi. The terms and conditions of the plan must be approved by the government of the country in which it is established and the failure to comply with such terms and conditions may result in the loss of registration and the preferential tax treatment afforded to the plan; and,

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- b. A trust, plan or other arrangement (“the plan”) that is accepted for registration, and qualifies under the tax law of the country in which it is established, for the purpose of fulfilling a social policy objective of the particular government, including but not limited to support for infirmity or disability, the advancement of education or retirement savings and which has all of the following attributes under such tax law:
 - i. The amount of the annual or cumulative life-time contributions to the plan are limited;
 - ii. The terms and conditions of the plan must be approved by the government of the country and the failure to comply with such terms and conditions may result in the loss of registration and the preferential tax treatment provided to the plan;
 - iii. Where contributions to the plan are deductible in computing the income of the contributor, withdrawals from the plan are required to be included in the income of the recipient thereof; and,
 - iv. Income and gains realized in respect of assets retained within the plan are not subject to tax until such income or gains are withdrawn from the plan, at which time the government may or may not subject such amounts to tax.