Notice 2009-17

Johnson Regina

From: Andrea Taylor [ataylor@iiac.ca]
Sent: Monday, March 16, 2009 3:34 PM
To: Notice Comments
Cc: Schaeffer Stephen J
Subject: Response to Notice 2009-17 - Investment Industry Association of Canada
Attachments: IIAC QI Notice 2009-17 FINAL.pdf

Please find attached in PDF format the comments of the Investment Industry Association of Canada on Notice 2009-17 (Information Reporting of Customer's Basis in Securities Transactions). We appreciate that the IRS is accepting these comments past the March 2, 2009 deadline set out in the Notice.

Please contact me if you have any questions or difficulties opening or reading the attachment.

Many thanks and best regards,

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

March 16, 2009

Stephen Schaeffer
Office of Associate Chief Counsel (Procedure & Administration)
CC:PA:LPD:PR (Notice 2009-17)
Couriers Desk
Internal Revenue Service
1111 Constitution Avenue, NW
Washington DC 20224

RE: Notice 2009-17: Information Reporting of Customer's Basis in Securities Transactions (the "Notice")

Dear Mr. Schaeffer:

Thank you for taking the time to speak with members of our Qualified Intermediary Committee on March 5, 2009. We appreciate the opportunity to provide further comment on the development of the new cost basis reporting regime, and to outline the complex challenges it will present for reporting foreign intermediaries.

The Investment Industry Association of Canada (**IIAC**) is Canada's equivalent to the Securities Industry and Financial Markets Association (**SIFMA**) in the United States, and represents over 200 investment broker-dealers across Canada. The IIAC QI Committee is responsible for reviewing and commenting on amendments to legislation that would affect the Canadian QI community, and developing positions on practical and conceptual matters surrounding US tax reporting requirements, including audits and QI forms.

Amendments to the Internal Revenue Code, Section 6045

The basis reporting amendments to Section 6045 (the "**Amendments**") of the Internal Revenue Code (the "**Code**") were passed as section 403 of Division B of H.R. 1424, the *Energy Improvement and Extension Act of 2008*. The Amendments require the reporting of a US customer's cost basis in a covered security as part of Form 1099-B, as well as identification of whether a capital gain or loss with respect to the security is long- or short-term. These reporting requirements will apply to securities acquired on or after the applicable date (as defined in the Code) or transferred into the account on or after the applicable date if basis information was provided by the transferor.

Background on Qualified Intermediaries

Revenue Procedure 2000-12, The Qualified Intermediary Agreement (the "**QI Agreement**") has been in effect since January 1, 2001. All foreign intermediaries entering into a QI Agreement are "Qualified Intermediaries" (**QIs**). A QI is a withholding agent and a payor under the Code for amounts that it distributes to its account holders. Except as otherwise provided in the QI Agreement, a QI's obligations with respect to distributions to account holders are governed by Chapters 3 and 61, and Section 3406 of the Code and the related regulations. There are approximately 6,500 QIs worldwide.

Section 8.04 of the QI Agreement sets out a QI's reporting responsibilities for a "reportable payment" other than a "reportable amount". Section 2.44 defines "reportable payment" as it applies to both US and non-US payors. In very general terms, proceeds of disposition realized on the sale of securities are included in the definition of "reportable payment" as follows:

- For a US payor, proceeds from the disposition of US and non-US securities are reportable payments as defined in section 3406(b) of the Code. There are also certain reporting obligations for dispositions by a US non-exempt recipient whose identity and account information is prohibited by law from disclosure as described in section 6.04 of the QI Agreement.

- For a non-US payor, proceeds from the disposition of US securities are reportable payments if sales are effected in the US within the meaning of Treas. Reg. section 1.6045-1(a), and proceeds from the disposition of non-US securities are reportable payments if payment is made in the US within the meaning of Treas. Reg. section 1.6049-5(e).

On this basis, Form 1099-B reporting of proceeds of disposition by a QI that is a non-US payor is generally only required for US non-exempt recipients residing in the US. Most Canadian QIs are non-US payors. As a result of various securities regulations and other compliance requirements, most QIs have a very limited number of accounts for US non-exempt recipients residing in the US. Given the proximity of Canada to the US and the mobility of individuals back and forth across the border, the Canadian QI community likely has a greater number of account holders for which the reporting of proceeds on Forms 1099-B is required than do QIs in other jurisdictions. Nevertheless, initial estimates by Canada's largest brokers indicated that less than 1% of their total accounts require Form 1099-B reporting of proceeds.

General Response to Notice 2009-17

We have had the benefit of reviewing comments already submitted by a number of US organizations in response to the Notice. Rather than reiterate many of the same points contained in these submissions that also apply to QIs, we have provided comments (see

Appendix "A") that focus on issues that relate specifically to the unique challenges faced by the QI community if we are required to comply with the Amendments.

The IIAC has previously provided comments to Tax Counsel of the House, Senate and Joint Committee on Taxation, as well as the Acting Tax Legislative Counsel in the Office of Tax Policy at the Department of Treasury. Although these comments remain applicable, we will not repeat all of them in detail in this submission. We are enclosing our earlier submissions for your reference (see Appendix "B").

SUMMARY OF RECOMMENDATIONS

1. Exclude QIs from the basis reporting requirements

There are a number of factors which support excluding QIs from the application of the Amendments.

a) Beyond the scope of the QI Agreement

The objective of the QI Agreement is set out in Revenue Procedure 2000-12:

> *The objective of the QI withholding agreement is to simplify withholding and reporting obligations for payments of income (including interest, dividends, royalties, and gross proceeds) made to an account holder through one or more foreign intermediaries.*

The cost basis of securities sold has no impact on the withholding obligations of a QI, nor does it impact the amounts to be reported with respect to income, including gross proceeds. We recognize that it is the right of the US government and the IRS to make changes to legislation. However, in many instances such changes will dramatically affect and alter the intent and scope of the QI contractual obligation. **It is our contention that extending the scope of a QI's information reporting obligation to include cost basis of securities sold is unwarranted and inappropriate without direct consultation with the QI community and an examination of the impact such changes bring.**

b) Excessive costs associated with compliance relative to potential additional tax revenue

As we have indicated above, securities and other compliance requirements limit the extent to which most QIs will have accounts for US residents. The aggregate amount reported on Forms 1099-B by QIs is likely negligible in relation to the amount reported by US paying agents. A review of Forms 1099-B actually submitted to the IRS would probably confirm this assumption.

The US tax rules associated with the calculation, maintenance and reporting of basis information are extremely complicated and must be supported by advanced systems capabilities and/or significant levels of manual record keeping. We understand that many

US brokers already have developed and implemented the necessary systems and process changes to provide some level of basis information and are voluntarily providing such information to account holders as a component of their customer service. Yet despite being further ahead in their ability to report basis information to the IRS, the comments already submitted in response to the Notice provide a clear indication that there are still a significant number of issues to be addressed in the guidance and regulations issued by Treasury and the IRS, for which US brokers will be required to develop further enhancements and modifications.

For QIs to comply with the Amendments, they will largely be starting from scratch, including from the perspective of having to research and become familiar with a new set of highly detailed and technical tax rules that have not previously had relevance to them. Significant systems, process and procedural enhancements would also be required. Those QIs that do currently provide customers with basis information are providing it in accordance with the rules applicable to the majority of their customers, which in Canada is the weighted average cost method. If these QIs are also required to comply with US basis calculation rules, this will be in addition to, rather than in lieu of, the information currently being maintained. All of this will be extremely costly for QIs that have very few accounts to which the rules apply.

The cost associated with developing, implementing and maintaining the capability and capacity to comply with the basis reporting requirements will likely exceed any additional tax revenue to be generated by additional information reporting provided by QIs and we strongly believe that QIs should be excluded from the requirements. If it can be demonstrated that there is in fact a potentially significant tax gap related to these accounts, the IRS and Treasury should consult with QIs to consider alternatives which would provide the IRS with increased information without being excessively burdensome for QIs.

2. If QIs are not excluded from the reporting requirements, defer applicable date

As discussed above, we strongly believe that QIs should be excluded from the basis reporting requirements, as the Amendments go beyond the intended purpose of the QI Agreement and because the cost associated with providing such information will not be offset by sufficient additional tax revenue.

It is clear from the contents of the Notice and the comments that have already been submitted, that there are a significant number of detailed issues that must be addressed by the IRS and Treasury prior to the release of meaningful guidance that will enable US brokers to implement basis reporting by the applicable dates. Deferring the application for QIs will allow the IRS to focus on the issues that impact US brokers reporting for the vast majority of US taxpayers.

If the IRS and Treasury determine that more time and/or information is required to confirm that excluding QIs from the application of the Amendments is the most

appropriate decision, we recommend that the applicable date of these provisions for QIs be deferred until there has been direct consultation with QIs.

REQUEST FOR FURTHER DISCUSSIONS

As mentioned during our call, the staff of the IIAC and members of our QI Committee would greatly appreciate the opportunity to discuss our issues in more detail with the IRS and Treasury, either in person or by conference call. I will contact you in the near future to discuss a convenient time for such a meeting.

In the meantime, if you have any questions or comments regarding our submission, please feel free to contact me by phone at 416-687-5477 or by email at JRando@iiac.ca.

Sincerely,

J. Rando

Jack Rando,
Director, Capital Markets
Investment Industry Association of Canada
www.iiac.ca

Encl.

cc: Douglas H. Shulman, Commissioner, Internal Revenue Service
Frank Ng, Commissioner, LMSB Division, Internal Revenue Service
Barry Shott, Deputy Commissioner – International, LMSB Division, Internal Revenue Service
Walter Harris, Industry Director, Financial Services, LMSB Division, Internal Revenue Service
Carl Cooper, Senior Counsel of the Office of Chief Counsel – International
Thomas Chillemi, QI Program Manager, LMSB Division, Internal Revenue Service
Eric San Juan, Acting Tax Legislative Counsel, Office of Tax Policy, Department of the Treasury

APPENDIX "A"

BASIS REPORTING REQUIREMENTS – ADDITIONAL CONSIDERATIONS FOR QUALIFIED INTERMEDIARIES

Numerous submissions providing comments in response to the Notice have already been received by the IRS and have set out details with which we are generally in agreement. We have therefore not repeated such comments in this appendix. Instead we have focused on highlighting issues that may be unique or more of a concern to QIs if required to comply with the Amendments.

1. Applicability of Reporting Requirements

a. Account holders that become US persons

As we have noted in this letter, and in our earlier submissions, the accounts for which most QIs are required to provide Form 1099-B reporting represent a negligible percentage of their overall population of accounts. If QIs are required to comply with the Amendments, most will likely rely heavily on the use of manual processes and can only reasonably maintain basis information for account holders for whom Form 1099-B reporting is required. **If an account holder becomes a US person, a QI should only be required to apply the Amendments to securities acquired or transferred into the account with a statement under section 6045A after the QI is notified that the account holder has become a US person. All other securities in the account should be treated as "uncovered securities".**

b. "Applicable person"

The definition of "applicable person" is relevant in the context of defining who is required to provide a broker with a statement containing transfer information under section 6045A. Only securities for which the broker has received such a statement are included in the definition of "covered securities" and therefore subject to the basis reporting requirements.

Several submissions have suggested that the list of applicable persons be expanded significantly to include such persons as transfer agents, investment advisers, trustees, etc., to provide brokers with basis information from a wider range of sources.

If securities are transferred to a QI, unless the transferor is another QI or US broker that also maintained basis information, most other transferors will likely be non-US persons who are unfamiliar with US tax rules and it would be unreasonable to expect them to provide a statement under section 6045A.

The definition of "applicable persons" should exclude non-US persons that were not required to file Forms 1099-B for the account from which the securities are

transferred, such that securities transferred to the broker from such persons will be "uncovered securities" for purposes of basis reporting.

c. Reporting of basis information for "uncovered securities"

In the case of "uncovered securities", a broker may have some basis information available which may have been received from external sources (including the account holder). Such information may or may not have been calculated in accordance with US tax rules. **The guidance should indicate whether or not a broker should provide whatever available basis information they may have for an uncovered security, provided there is no reason to believe that the amounts are unreasonable.** If the IRS would prefer to have whatever information is available, it should be recognized that the amounts are provided for information purposes only and that the broker is not responsible for the accuracy of the amounts provided. Amendments to the Form 1099-B should allow the broker to indicate whether the securities disposed of were covered or uncovered and what method was applied for purposes of calculating basis.

d. Issuer's Classification of Securities

If QIs are subject to the Amendments, it should be recognized the majority of the investments held in customers' accounts will likely be non-US securities. Non-US issuers are generally unlikely to provide information regarding the US taxation of a non-US instrument, including the classification of the security for US tax purposes. Many such securities may also be structured such that there is no US equivalent, further complicating efforts to classify and calculate basis in accordance with US tax rules. **Brokers who are unable to obtain US tax classification information for a security should be permitted to use their best efforts to make a reasonable determination and should not be penalized if it is later determined that the security was incorrectly classified.**

e. Applicable Dates for Covered Securities

If QIs are not be excluded from the new requirements, they should be granted a reasonable extension of the 'applicable dates'.

In addition, for some QIs, the implementation of the new requirements will be further complicated by staggered applicable dates which are dependent upon the classification of the instrument. **We would recommend that QIs have the option of reporting basis for all types of securities from the first extended 'applicable date'.**

2. Basis Method Elections

We share the concerns expressed in the submissions of other organizations that "maximizing" customer flexibility with respect to the selection of reporting options may not be compatible with the goal of minimizing broker burden. For QIs, this burden will

be even more disproportionate to the potential benefits to be derived by customers or the IRS.

As we have indicated in previous submissions, many QIs do not currently have systems that maintain basis information or they provide such information as a customer service only, qualifying the accuracy of the information being provided. Canadian QIs that provide basis information use a weighted average cost method as required for Canadian income tax purposes. Other calculation methods may be used by QIs in other jurisdictions.

Most QIs currently have no systems in place for providing information calculated in accordance with a single acceptable US method, let alone providing customers with the option of selecting different methods, not only at the account level, but also for selected securities within their accounts.

It is our recommendation that QIs, if not excluded from the Amendments, should be permitted to report cost calculated in accordance with the method already in place, or such other method as is commonly used in their jurisdiction. The onus should be on the customer to reconcile the amounts reported by the QI with the amounts to be reported on their US tax returns, using transaction and other statements that the QI provides on a regular basis. These statements should also be sufficient to permit the customer to identify capital gains as long or short-term. However, even this type of reporting would require implementing changes to systems for the sake of reporting on a very small number of accounts and we feel the more appropriate conclusion would be to totally exclude QIs from cost basis information reporting.

If QIs are not excluded from the Amendments and are not permitted to calculate basis using a method already being applied or most commonly used in their jurisdiction, **they should only be required to calculate using a default method deemed acceptable by the IRS, and they should not be required to offer customers the option of electing alternative methods.** If customers wish to apply an alternative method, they should be responsible for providing a reconciliation between the amount reported by the QI and the amount reported on Schedule D of their Form 1040 return.

3. Dividend Reinvestment Plans

If QIs are not excluded from the Amendments, it must be recognized that in Canada, mutual funds are generally structured as trusts and are very popular investment vehicles. Many investors arrange to have distributions automatically reinvested to acquire additional units. **The description of arrangements qualifying as dividend reinvestment plans should be broadened to include arrangements available in foreign jurisdictions that are similar to DRIPs.**

4. Reconciliation with Customer Reporting

Again, we concur with the opinions expressed by our colleagues in the US, namely, that it is not feasible or practical for brokers to take on the responsibility of ensuring consistency between broker reporting on Form 1099-B and customer reporting on Schedule D of Form 1040. Reporting brokers can provide additional communications and instructions as to how information can be used and maintained by customers, but should not be responsible for reconciliation. **The onus should be on the customer to reconcile the amounts reported on Forms 1099-B with the amounts to be reported on their US tax returns, using the transaction and other statements provided by their brokers on a regular basis.**

5. Special Rules and Mechanical Issues

A number of comments have already been provided in other submissions in regards to points under "Special Rules and Mechanical Issues". QIs will also encounter additional issues as a result of their holdings in non-US securities that may include post year-end and other basis adjustments. ***De minimus*** **thresholds should be introduced to remove the requirements to adjust basis for smaller amounts, particularly when amounts are not determinable until after the initial reporting deadline. QIs should not be penalized if reasonable efforts are made to determine the impact of such adjustments on US tax basis.**

6. Transfer Reporting

We understand that US brokers have the benefit of uniform broker-to-broker information standards (ACTS) and the Cost Basis Reporting System (CBRS) maintained by DTCC to facilitate the transfer of basis information between brokers. It is unlikely that electronic reporting will be an option for most QIs. Because of the low volume of accounts that will likely transfer during a year, and because transfers may also involve QIs in different jurisdictions, it is unlikely that standard processes for transferring information will develop. The transfer of information in these situations will likely depend on manual procedures. **Delays in the transfer of information should not be subject to penalties if the transferring QI has made best efforts to provide details in a timely manner.**

7. Issuer Reporting

As noted above, the majority of securities held by most QIs are likely to be issued by non-US entities. Non-US issuers will generally not provide information regarding the US tax consequences of corporate actions. **We reiterate the point made above that QIs should not be penalized if reasonable efforts are made to determine the impact of corporate actions on basis if no information is provided by issuers.**

8. Broker Practices and Procedures

Although information contained in the Administration's Fiscal Year 2009 Revenue Proposals indicates that, under regulations, a broker would not be penalized for failure to accurately report items of information that the broker is unable to obtain with "reasonable efforts", it is not clear what will be considered a "reasonable effort" in any particular instance. While administrative relief is welcome, we believe that the term "reasonable efforts" should be clearly defined under the regulations. **We recommend that there should be transitional relief from reporting penalties for at least two years after the reporting requirements take effect, and that the IRS should generally exercise discretion when imposing any penalties for failure to comply with the new basis reporting rules.**

APPENDIX "B"

PREVIOUS IIAC SUBMISSIONS

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

January 9, 2009

Eric A. San Juan
Acting Tax Legislative Counsel
Office of Tax Policy
Department of the Treasury
1500 Pennsylvania Avenue NW
Washington, DC 20220

Dear Mr. San Juan:

Re: Securities Basis Reporting by Qualified Intermediaries (QIs)

I thank you and your colleagues for taking the time to speak with me and members of our Association's Qualified Intermediary Committee on October 8, 2008. During that conference call, we were asked to draft a letter outlining our interpretation of the amendments to Internal Revenue Code (the "**Code**"), Section 6045, and how these amendments would adversely impact QIs. In addition, we were asked to locate the source of the authority for the Treasury Department to draft regulations to accompany the amendments that would effectively exclude QIs from the new reporting requirements, and to suggest draft language that might be included in such regulations.

The Investment Industry Association of Canada (**IIAC**) is Canada's equivalent to the Securities Industry and Financial Markets Association (**SIFMA**) in the United States. All but a few of Canada's over 200 investment broker-dealers are members of the IIAC. The IIAC QI Committee is responsible for reviewing and commenting on amendments to legislation that would affect the Canadian QI community, and developing positions on practical and conceptual matters surrounding U.S. tax reporting requirements, including audits and QI forms.

Background on Qualified Intermediaries

Revenue Procedure 2000-12, The Qualified Intermediary Agreement (the "**QI Agreement**") has been in effect since January 1, 2001. All foreign intermediaries entering into the QI Agreement are "Qualified Intermediaries" (**QIs**). A QI is a withholding agent under Chapter 3 of the Code, and a payor under Chapter 61 and Section 3406 of the Code for amounts that it distributes to its account holders. Except as otherwise provided in the QI Agreement, a QI's obligations with respect to distributions to account holders are governed by Chapters 3 and 61 and Section 3406 of the Code and its related regulations. There are approximately 6,500 QIs worldwide.

Amendments to Internal Revenue Code, Section 6045

The basis reporting amendments to Section 6045 of the Code were passed as section 403 of Division B of H.R. 1424, the *Energy Improvement and Extension Act of 2008* (the "**Amendments**"). The Amendments require the reporting of a U.S. client's adjusted cost basis in a covered security[1] as part of Form 1099-B, as well as identification of whether a gain or loss with respect to the security is long- or short-term. These reporting requirements will apply to securities acquired on or after the effective date or transferred into the account on or after the effective date if basis information was provided by the transferor. The effective date is January 1, 2011 for stock in a corporation, January 1, 2012 for stock in open-end mutual funds and dividend reinvestment plans, and January 1, 2013 for other securities.

Challenges Faced by Canadian QIs Relating to the Amendments

Given the proximity of Canada to the U.S., and the mobility of individuals back and forth across the border, one would assume that the Canadian QI community is likely to have a greater number of accountholders for whom the reporting of proceeds on Form 1099-B is required, than do QIs in other jurisdictions. However, our initial analysis clearly indicates that Canadian QIs do not have a significant number of such accountholders. Our analysis, based on estimates compiled from a sample of our largest member firms, found that the number of accountholders for whom reporting of proceeds is required is significantly less than 1% of their total number of accounts that are subject to their QI Agreements.

Given the small number of accountholders for whom basis reporting will likely be required, it is unlikely that QIs will be able to justify making the complex and very costly system changes that would be required to fully automate the calculation and maintenance of cost-basis information for the purposes of satisfying the reporting requirements of the Amendments. As a result, alternative solutions that require greater reliance on manual procedures will likely be necessary, still with a very significant cost to the QIs that will almost certainly have no ability to recover related costs from the client.

No or Limited Basis Calculations Currently Performed

Many QIs do not currently have systems that maintain basis information or they provide such information as a client service only, qualifying the accuracy of the information being provided. The reliability of the information is frequently limited by many factors that lie outside of the control of the brokers, including the accuracy of information that is provided by previous brokers for assets transferred to the client's account. Significant enhancements to systems and procedural changes would be required to refine the accuracy of the information provided. Given the small estimated number of clients for

[1] "Covered Security" includes any stock, note, bond, debenture or other evidence of indebtedness, commodity, contract or derivative with respect to the commodity, or any other financial instrument that is determined to be appropriate by the Secretary.

whom such reporting would be required, the QI may need to rely on manual processes and procedures.

Multiple Basis Calculation Methods

Canadian QIs that are providing cost basis information for Canadian securities use the weighted average cost method as required for Canadian income tax purposes (other calculation methods may be used by QIs in other jurisdictions). For this reason, Canadian QIs would need to maintain at least two types of tracking systems. In addition to the calculation of cost being different for Canadian and U.S. reporting purposes, the U.S. calculations are further complicated by rules that apply different methods to different types of assets, and also allow individual taxpayers to make their own elections as to the method of calculation to be used. The requirement to separately report short- and long-term capital gains (based on U.S. tax requirements) would add an additional element of cost and complexity.

Foreign Currency Exchange

The calculations are further complicated by foreign currency exchange. For many account holders with accounts outside the U.S., the base currency of the account will not be in U.S. dollars. Additional currency conversion information will be needed if cost basis must be determined in U.S. dollars based on the exchange rate in effect at the time of the transaction, which could vary significantly between brokers based on the source of their rate information.

Determination of U.S. Tax Implications of Corporate Actions

Corporate actions are currently processed in accordance with tax laws or standard industry practices applicable in the QI's jurisdiction. There will be a significant cost associated with determining the U.S. tax implications of the event on the cost of a U.S. taxpayer's holdings, as well as posting the event differently for U.S. tax purposes. This is further complicated by the fact that a large portion of the securities held by QIs are non-U.S. and information regarding the U.S. implications of an event may not be readily available.

Basis Calculations Impacted by Non-Cash Amounts

The cost of certain types of investments is not necessarily based on cash payments. For example, the cost of a partnership interest is based on the investor's share of the partnership's income or loss, as well as contributions to and withdrawals from the partnership. For other investments, distributions may automatically be reinvested without the payment of cash. Custodians do not have the information required to maintain cost basis information in these situations.

Existing Accountholders that Become U.S. Persons

Given initial findings that suggest that basis reporting might be required for less than 1% of a QI's client base, it is unlikely that the calculation process and data retention can be automated. Based on this premise, it would only be practical for a QI to maintain such information for those clients that become U.S. persons for securities acquired or transferred after the date that the QI is aware of the change in status, unless cost at the time of becoming a U.S. person can be used in all such situations.

Filing Deadline

Although the Amendments extend the Form 1099 filing deadline from January 31 to February 15, the timelines remain extremely tight for QIs, especially in the following instances:

- Where there has been a corporate action for which the issuer is required to provide additional information;
- Where there has been a transfer of securities late in the year for which the transferor must provide cost basis information by January 15, following the year-end;
- For holdings such as certain Canadian mutual funds, for which a portion of distributions may be a return of capital, impacting cost basis, but for which the information is not often available prior to February 15, or later;
- For reinvestment amounts for the many investments with automatic dividend reinvestment plans for which the amounts are often not identified until after year-end.

Transfer of Basis Information Between Brokers

Based on earlier discussions related to the small percentage of account holders for whom reporting would be required, if QIs are dependent on manual procedures to calculate, track and report U.S. cost basis, it will be very difficult to develop a standard method for efficiently transferring cost information within 15 days of the transfer when shares are transferred from one broker to another or from one QI to another.

Reconciling Differences with Accountholders

Despite best efforts on the part of the QI to provide accurate cost basis information, it is inevitable that there will be discrepancies between the amounts determined by the QI and the amounts determined by its account holders. Considerable resources will be consumed addressing these differences with account holders, and most likely at a time when these resources are otherwise engaged in year-end reporting activities. In addition to the heavy demand on resources, despite all efforts by the QI, these differences are often likely to result in friction and unnecessary client dissatisfaction with no easy solution.

Procedures Under Section 3.05 of the QI Agreement

Under Section 3.05 of the QI Agreement, a QI that has not assumed backup withholding and Form 1099 reporting responsibilities can request another payor to report and, if required, backup-withhold on broker proceeds. Other payors that have agreed to take on this reporting and withholding responsibility may not have the ability to provide cost basis reporting, depending on the structure of the QI's accounts with the payor.

Relief from Reporting Penalties

Although information contained in the Administration's Fiscal Year 2009 Revenue Proposals indicates that, under regulations, a broker would not be penalized for failure to accurately report items of information that the broker is unable to obtain with "reasonable efforts", it is not clear what will be considered to be a reasonable effort in any particular instance. While administrative relief is welcome, we believe that the term "reasonable efforts" should be clearly defined under the regulations. We also recommend that there should be transitional relief from reporting penalties for two years after the reporting requirements take effect.

The Authority for Treasury to Draft Regulatory "Carve-Out" Provisions for QIs

Paragraph 6045(a) of the Code provides a broad authority for Treasury to draft regulations and forms with respect to the reporting requirements of Section 6045:

> Every person doing business as a broker shall, **when required by the Secretary**, make a return, **in accordance with such regulations as the Secretary may prescribe**, showing the name and address of each customer, with such details regarding gross proceeds, and such other information **as the Secretary may by forms or regulations require** with respect to such business. (**emphasis added**)

We understand that Treasury must draft regulations that reflect the purpose and intent of legislation, and it is our position that drafting regulations that exclude QIs from the cost basis reporting requirements would not be a derogation from the intent of the Amendments. The legislation was adopted to improve compliance related to the reporting of capital gains and losses realized on dispositions of securities by U.S. individual taxpayers, the bulk of which will be captured by the reporting submitted by U.S. brokers. This legislation potentially extends the application of cost basis reporting to QIs, which would seem to go beyond the intent of the legislator, and should be excluded by regulations because of the unduly burdensome nature of the requirements, particularly in relation to the nominal contribution that will be made to increasing compliance by U.S. individuals.

GAO-06-603 recommended that cost basis reporting be implemented to reduce the capital gains tax gap, but recognized that cost basis reporting would "raise challenges that would need to be addressed...brokers would incur costs and burdens...and many issues would arise about...which securities would be covered." This suggests that when the

GAO made its recommendations regarding legislation, flexibility was contemplated in how the basis reporting requirements should be applied, and recognized that these requirements might not be appropriate for some types of securities, or, as we would argue, for some types of filers of Forms 1099-B.

In April 2007, Eric Solomon, the Assistant Secretary for Tax Policy testified before the Senate Finance Committee, stating that "the Administration is committed to reducing the tax gap without unduly burdening honest taxpayers who currently meet their tax obligations." We contend that imposing the cost basis reporting requirements on QIs would be unduly burdensome by forcing the QIs to incur high costs of compliance, which are unlikely to be recouped from clients. Furthermore, based on our initial estimates that basis reporting would be applicable to a very small number of accountholders, this would likely result in little or no change to the U.S. tax gap. This is precisely the type of situation that warrants the drafting of a regulation to create an exemption for QIs.

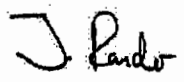
Proposed Regulations

It is difficult for us to suggest draft language to implement such an exemption without first reviewing any proposed regulations that Treasury is drafting with respect to the Amendments. We would be pleased to review any draft regulatory language once it has been prepared, to ascertain how best to insert relief that would carefully exclude QIs from the cost basis reporting requirements and not create loopholes that could be inappropriately exploited by others, undermining the purpose of the Amendments.

Request for further discussions

The staff of the IIAC and the members of our QI Committee would very much appreciate the opportunity to discuss our issues with the Treasury Department, and answer questions or assist with the development of draft regulations excluding QIs from the requirements contained in the Amendments. During the conference call on October 8, 2008, it was mentioned that there may be hearings on this matter, and we would appreciate receiving any information available on where and when we might be able to present our information and arguments to ensure that those who are drafting the regulations understand the reasons for, and the importance of, our request.

Yours truly,



Jack Rando
Director, Capital Markets
Investment Industry Association of Canada

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

Barbara Amsden
Director, Capital Markets
Tel: (416) 687-5476
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June 6, 2008

Ms. Catherine Koch
Chief Tax Counsel, Committee on Finance
219 Dirksen Senate Office Building
Washington, DC 20510-6200
Tel: (202) 224-4515
Fax: (202) 228-0554

Dear Ms. Koch:

Re: Urgent Request for Meeting on Basis Proposals

John Buckley, Majority Chief Tax Counsel, met with the Chair and Vice-Chair of the Qualified Intermediary Committee of the Investment Industry Association of Canada ("IIAC") and me on June 2, 2008 regarding the basis reporting proposals that have passed from the House of Representatives to the U.S. Senate as part of *American Housing Rescue and Foreclosure Prevention Act of 2008* (H.R. 3221). He had been unaware that the provisions would affect foreign intermediaries and suggested we contact you with our request that a provision be added to give Treasury regulatory authority to provide for limited exceptions to exclude, if justified, foreign intermediaries from being subject to the rules and to deal with them separately. **Could we arrange a call with you as soon as possible to discuss our concerns regarding basis reporting proposals under Internal Revenue Code s. 6045?**

The IIAC is Canada's equivalent to the U.S. Securities Industry and Financial Markets Association. All but a handful of Canada's 200 investment dealers are members, and all larger Canadian investment dealers (based on size of assets under custody) have entered into Qualified Intermediary Agreements with the U.S. Internal Revenue Service ("IRS").

Qualified Intermediaries

Revenue Procedure 2000-12, *The Qualified Intermediary Agreement*, has been in effect since January 1, 2001. All foreign intermediaries entering into this Agreement with the Internal Revenue Service are Qualified Intermediaries ("QIs"). A QI is a withholding agent under chapter 3 of the Code and a payor under chapter 61 and section 3406 of the Code for amounts that it pays to its account holders. Except as otherwise provided in the Agreement, a QI's obligations with respect to amounts paid to account holders are governed by chapter 3, chapter 61 and section 3406 of the Internal Revenue Code and related regulations. There are approximately 6,500 QIs throughout the world.

Among the global QI population, Canadian QIs (which also include Canada's largest banks and custodians) will likely be most affected by the basis reporting proposals due to the proximity of our two countries, but even here, clients for whom the proposals would apply represent less than one per cent of our members' total number of accounts subject to their QI Agreements. Restrictions on Canadian brokers servicing clients in the U.S. limit the number of U.S. resident account holders – for one of the top 10 Canadian firms, U.S. residents' accounts that would be captured by the basis proposals represent only .13 of one per cent of all accounts at the firm (a ratio of .0013:1).

Canadian QIs, more so than QIs in other jurisdictions, are likely to have accounts for U.S. non-exempt recipients for which the QI is required under the terms of the QI Agreement to report sales proceeds for both U.S. and non-U.S. assets. As it is, Canada's population, at barely 10 per cent of the U.S.'s, often makes provision of new services or implementation of new requirements uneconomic due to lack of economies of scale.

Why foreign intermediaries have problems

You will find enclosed our correspondence to John Buckley and others, which explains our concerns with the proposed legislation and our members' obligations as Qualified Intermediaries in greater detail, however, the most serious additional challenges QIs will face that U.S. firms will not include:

- Canadian tax law requires use of the weighted average cost method for tax purposes, while U.S. law demands the first in/first out method.

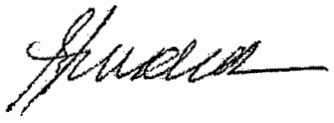
- Canadian tax law, in contrast to U.S. tax law, does not allow different methods to be used for different types of assets, does not permit individual taxpayers to elect to use different methods, does not require short- and long-term capital gains to be treated differently and does not require different calculations for corporate actions taking place in other countries.

- Calculations would be required in U.S. dollars, which further complicates basis calculations for QIs that are likely maintaining a large number of their accounts in other base currencies.

As the same client could require different bases on different assets, payments to be treated in different ways, different currencies, and different treatment for tax and securities regulatory purposes, the programming scenarios increase exponentially for a very small percentage of clients.

The basis reporting provisions were discussed with U.S. industry groups for quite some time, however, most of the Canadian QI community only became aware of these provisions in early 2008. Patty McClanahan of SIFMA is aware of and had no concerns with our efforts to seek an amendment to give Treasury authority to provide for limited exceptions to deal separately with foreign intermediaries. This would allow time for consultation to understand the additional challenges faced by foreign intermediaries, and to discuss alternatives and timeframes. I will call you shortly to seek a convenient time to meet with you.

Yours truly,



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

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February 22, 2008

Mr. Russ Sullivan
Democratic Staff Director
Mr. Kolan L. Davis
Republican Staff Director
Mr. Mark Prater
Republican Chief Tax Counsel
Senate Committee on Finance
Mr. Edward Kleinbard
Chief of Staff, Joint Committee on Taxation
219 Dirksen Senate Office Building
Washington, DC 20510-6200

Mr. John L. Buckley
Majority Chief Tax Counsel
Mr. Jon Traub
Minority Chief Tax Counsel
House Committee on Ways and Means
1110 Longworth House Office Building
Washington, D.C. 20515

Dear Sirs:

Re: IIAC Comments on Basis Reporting Proposals under Internal Revenue Code S. 6045

The Investment Industry Association of Canada (IIAC) would like to comment, on behalf of the Canadian Qualified Intermediary (QI) community, on the basis reporting proposals under section 6045 of the Internal Revenue Code as currently contained in the *Administration's Fiscal Year 2009 Revenue Proposals* and tax title of H.R. 6, *the Clean Renewal Energy and Conservation Act of 2007*, and also as evidenced in H.R. 3996, *Temporary Tax Relief Act of 2007*. The proposals would require reporting of a client's adjusted cost basis in a covered security – stocks; notes, bonds, debentures or other evidence of indebtedness; any commodity, contract or derivative with respect to the commodity; and any other financial instrument for which the Secretary determines that basis reporting is required – as well as identification of whether a gain or loss with respect to the security is long- or short-term. These requirements are scheduled to apply to stocks (including investments in regulated investment companies or RICs) acquired or transferred on or after Jan. 1, 2009, and to all other securities on or after Jan. 1, 2011.

Our members not only share the concerns expressed by U.S. organizations in regard to these proposals, but also have serious additional concerns more particular to QIs and other foreign intermediaries. We urgently request that the proposed legislation be amended to exclude QIs and other foreign intermediaries altogether or as a minimum that Treasury be given broad regulatory authority to carve them out or set rules recognizing the particular difficulties they face.

Treasury Secretary Paulson said that his goal "... is to promote the conditions for American prosperity and economic growth – and maintaining the competitiveness of [U.S.] capital markets is central to that goal." Capital markets and tax systems are connected. We believe that implementing tax provisions that will force foreign intermediaries to incur significant costs for a very small client base risks adding to current challenges to the pre-eminence of American capital markets. We therefore request that the proposed legislation be amended and that rules applicable to foreign intermediaries be addressed separately for the reasons outlined below.

General Recommendations

1. **Provide for Regulatory Authority to Exclude QIs.** We fully support the recommendation made by the Securities Industry and Financial Markets Association (SIFMA) in its June 28, 2007 letter to Russ Sullivan and Kolan Davis, specifically that Treasury should be given broad regulatory authority to implement the new requirements and, in particular, to provide for limited exceptions if justified. ***Treasury should have the authority to exclude QIs (and other foreign intermediaries) from being subject to the rules as proposed and to deal with them separately from U.S. brokers due to the different challenges they face.***

2. **Consult with QIs Due to Additional Challenges Faced by QIs.** In addition to the concerns and complications with the proposals that have been raised by U.S. brokers – all of which apply equally to QIs – there a number of additional challenges, which the proposals present for QIs that are less likely to impact U.S. brokers. Some of these challenges, listed in Appendix A, add cost and complexity for QIs, while the amount of additional tax revenue that is likely to be collected as a result of requiring QIs to report basis information is limited, as discussed further below in Background Information Regarding QIs. We would appreciate the opportunity to work with the Treasury Department and IRS to ensure that the potential tax revenue gains and costs associated with providing the information are assessed, and that all reasonable alternatives are fully considered. ***Before any legislation requiring basis reporting by QIs is introduced, we believe that there should be consultation with the QI community. We would welcome the opportunity to work with the Treasury Department and IRS to ensure that interests of all parties are taken into account and that a reasonable solution is developed.***

3. **Defer Effective Date.** We agree with SIFMA's recommendation that the effective date of any new reporting requirements should be based on finalization of Treasury regulations. As noted in SIFMA's submission, "Brokers cannot develop or modify their basis reporting systems if they do not know the rules they must follow." Moreover, given the complexity of basis reporting and depending on the nature of any requirements that might be implemented, 18 months may not be sufficient. ***We recommend that the effective date of any new reporting requirements applicable to QIs be based on finalization of Treasury regulations and that a reasonable effective date, including a phased implementation, be determined through consultation with QIs.***

4. **Recognize Taxpayer Responsibility.** Although we acknowledge that it would be efficient to have brokers report basis information related to dispositions by U.S. non-exempt recipients as a means of verifying gains and losses reported by taxpayers, the efficiency will be lost if the cost to brokers is excessive and, despite the brokers' best efforts, calculations are inaccurate. Taxpayers have an obligation to retain the information supplied by their broker that supports their cost calculations. It seems particularly unfair to shift this burden to a foreign financial institution to which data is not available. If a U.S. person residing in the U.S. makes a decision to use the services of a foreign financial institution, it should be recognized that the foreign financial institution may not be able to provide all information in the format that a U.S. taxpayer requires and that the taxpayer therefore may have to assume greater responsibility and cost with respect to recordkeeping. ***We strongly recommend that foreign financial institutions be excluded from basis reporting obligations.***

Background Information Regarding QIs

The majority of Canadian QIs are non-U.S. payors, and have assumed non-resident alien (NRA) withholding and backup withholding and 1099 reporting responsibilities. Section 8.04 of the QI Agreement sets out the Form 1099 reporting responsibilities of a QI. With respect to QIs that have assumed backup withholding and 1099 reporting responsibilities (i.e., "withholding QIs"), Form 1099-B reporting of proceeds is addressed in section 8.04(d) of the

Agreement, which requires the QI to file Form 1099 for a "reportable payment" other than a "reportable amount". These reporting obligations also apply to a QI that has not assumed backup withholding and Form 1099 reporting responsibilities (i.e., a "non-withholding QI") unless, under the procedures of section 3.05 of the Agreement, another payor has agreed to undertake the reporting and backup withholding as required and the QI does not know that the other payor has failed to withhold or report. Section 2.44 of the QI Agreement defines "reportable payment" in the case of a non-U.S. payor.

Although there are exceptions, in very general terms, the obligations of a non-U.S. payor QI to report proceeds are generally limited to the sale of securities by U.S. non-exempt recipient accountholders residing in the U.S. and either:

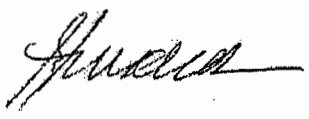
1. in the case of U.S. securities, regularly transmitting instructions from within the U.S. to the QI or
2. in the case of non-U.S. securities,
   - regularly transmitting instructions from within the U.S. to the QI or
   - receiving confirmation of the sale by mail to an address in the U.S.

Given the proximity of Canada to the U.S. and the mobility of individuals back and forth across the border, the Canadian QI community is likely to have a greater number of accountholders for whom the reporting of proceeds on Forms 1099-B is required than do QIs in other jurisdictions. Nevertheless, initial analysis indicates that even Canadian QIs do not have a significant number of such accountholders. Two of the largest Canadian brokers found, based on initial estimates, that the number of accountholders for whom reporting of proceeds was required was less than one per cent of their total number of accounts subject to their QI Agreements.

Given the small number of accountholders for whom basis reporting will likely be required, it is unlikely that QIs will be able to cost-justify making the complex and costly systems changes that would be required to fully automate the calculation and maintenance of cost-basis information for purposes of satisfying the proposed reporting requirements. As a result, alternative solutions that require greater reliance on manual procedures will likely be required, still with a significant cost to the QIs that will almost certainly have no ability to recover related costs from the client.

The brief summary of some of the challenges faced by QIs if they are required to provide basis reporting to those accountholders receiving Forms 1099-B reporting proceeds of disposition is provided in Appendix A to this letter. We would very much appreciate the opportunity to meet with Treasury Department and IRS staff directly to provide additional details supporting the need to exclude QIs and other foreign intermediaries from the basis reporting requirements as they are currently drafted, and to discuss alternatives.

Yours truly,



APPENDIX A

SUMMARY OF SOME CHALLENGES RELATED TO BASIS REPORTING BY QIS

No or Limited Basis Calculations Currently Performed. Many QIs do not currently have systems that maintain basis information or they provide such information as a client service only, qualifying the accuracy of the information being provided. The reliability of the information is frequently limited by a number of factors, including the accuracy of information that is provided by previous brokers for assets transferred to the client's account. Significant enhancements to systems and procedural changes would be required to refine the accuracy of the information provided. Given the estimated number of clients for whom such reporting would be required – two large firms estimate that the proposals would apply to less than one per cent of their client base, the QI may need to rely on manual processes and procedures.

Multiple Basis Calculation Methods. Canadian QIs that are providing basis information calculate cost using the *weighted average cost method* as required for Canadian income tax purposes (other calculation methods may be used by QIs in other jurisdictions). For this reason, Canadian QIs would need to maintain at least two types of tracking systems. In addition to the calculation of cost being different for Canadian and U.S. reporting purposes, the U.S. calculations are further complicated by rules that apply different methods to different types of assets, and also allow individual taxpayers to elect to use different methods. The requirement to separately report short- and long-term capital gains (based on U.S. tax requirements) would add an additional element of cost and complexity.

Foreign Exchange. The calculations are further complicated for foreign exchange translation reasons. For many accountholders with accounts outside the U.S., the base currency of the account will not be U.S. dollars. Additional information will need to be maintained if cost must be determined in U.S. dollars based on the exchange rate in effect at the time of the transaction, which could vary between parties based on the source of their rate information.

Determination of U.S. Tax Implications of Corporate Actions. Corporate actions are currently processed in accordance with tax laws or standard industry practices applicable in the QI's jurisdiction. There will be a significant cost associated with determining the U.S. tax implications of the event on the cost of a U.S. taxpayer's holdings, as well as posting the event differently for U.S. tax purposes. This is further complicated by the fact that a large portion of the securities held by QIs are non-U.S. and information regarding the U.S. implications of an event may not be readily available.

Basis Calculations Impacted by Non-Cash Amounts. The cost of certain types of investments is not necessarily based on cash payments. For example, the cost of a partnership interest is based on the investor's share of the partnership's income or loss, as well as contributions to and withdrawals from the partnership. For other investments, distributions may automatically be reinvested without the issuance of cash. Custodians do not readily have the information required to maintain tax cost information in these situations.

Existing Accountholders that Become U.S. Persons. Given initial findings that suggest that basis reporting might be required for less than one per cent of a QI's client base, it is unlikely that the calculation process and data retention can be automated. On that basis, it would only be practical for a QI to maintain such information for those clients to whom the reporting is required. This creates potential problems in the case of clients that become U.S. persons at a later date, unless cost at the time of becoming a U.S. person can be used in all such situations.

Filing Deadline. Although the proposed legislation extends the Form 1099 filing deadline from January 31 to February 15, the timelines remain very tight for QIs. This is particularly true:

- where there has been a corporate action for which the issuer is required to furnish additional information
- where there has been a transfer of securities late in the year for which the transferor must furnish basis information by January 15 following year-end
- for holdings such as certain Canadian mutual funds, for which a portion of distributions may be a return of capital, impacting cost basis, but for which the information is not often available prior to February 15 or later
- for reinvestment amounts for the many investments with automatic dividend reinvestment plans for which the amounts are often not identified until after year-end.

Transfer of Basis Information between Brokers. Based on earlier discussions related to the small percentage of accountholders for whom reporting would be required, if QIs are dependent on manual procedures to calculate, track and report U.S. cost, it will be difficult to develop standard methods for efficiently transferring cost information when shares are transferred from one QI to another. While we agree with SIFMA's concerns regarding a delay of up to 45 days for the transfer of this information, in other respects this may not be long enough to allow the transferring broker to complete the calculations.

Reconciling Differences with Accountholders. Despite best efforts on the part of the QI to provide accurate basis information, it is inevitable that there will be differences between the amounts determined by the QI and its accountholders. Considerable resources will be consumed addressing these differences with accountholders, and most likely at a time when these resources are otherwise engaged in year-end reporting activities. In addition to the demand on resources, despite all efforts by the QI, these differences are often likely to result in friction and client dissatisfaction with no easy solution.

Procedures under Section 3.05 of the QI Agreement. Under Section 3.05 of the QI Agreement, a QI that has not assumed backup withholding and Form 1099 reporting responsibilities can request another payor to report and, if required, backup-withhold on broker proceeds. Other payors that have agreed to take on this reporting and withholding responsibility may not have the ability to provide basis reporting, depending on the structure of the QI's accounts with the payor.

Relief from Reporting Penalties. Although information contained in the Administration's Fiscal Year 2009 Revenue Proposals indicates that, under regulations, a broker would not be penalized for failure to accurately report items of information that the broker is unable to obtain with reasonable efforts, it is not clear what will be considered to be a reasonable effort in any particular instance. While administrative relief is welcome, we believe that the term "reasonable efforts" should be clearly defined under the regulations. We also agree with SIFMA's recommendation that the statute should provide transitional relief from reporting penalties for two years after the reporting requirements take effect.