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Director

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SENT VIA EMAIL

Re: Urgent Request for Discussion of the Implications of the Foreign Account Tax Compliance Act (FATCA) on the Capital Markets Business Sector

Dear Sirs:

The Investment Industry Association of Canada (IIAC)[1] is writing this letter to further clarify issues that have been brought to our attention in relation to business units of our members involved in investment banking, proprietary trading and funding, syndications, securitizations, derivatives, notional principal contracts, securities lending, sale/repurchase transactions, commodities trading and fixed income trading (collectively, the "capital markets" businesses). We appreciate the opportunity to speak with you about our recommendations for dealing with these matters in a way that will achieve the policy goals of FATCA while allowing financial institutions adequate time to

[1] IIAC is Canada's equivalent to the Securities Industry and Financial Markets Association (SIFMA) in the United States, and represents approximately 95% of all investment dealers across Canada - 180 bank-owned and independent firms in total. Our members manage over $900 billion in assets for their clients in 9.8 million brokerage accounts. More information and a list of members is available at http://www.iiac.ca.

deal with implementation challenges.

Recommendations

We believe that steps should be taken to implement the following solutions as soon as possible, in order to alleviate potential disruption and increased risk to international capital markets:

1. Guidance should be released that provides for symmetry in the application of FATCA to Foreign Financial Institutions (FFIs) and United States Financial Institutions (USFIs), particularly with respect to passthru payments. It is critical to immediately address this issue with regard to Master Agreements (as defined herein) in order to avoid disrupting the ordinary course of business in the derivatives market.

2. Guidance should be provided as soon as possible to identify any payments under Master Agreements that are ***not*** included in the scope of the passthru payment provisions. This would alleviate Participating FFIs (PFFIs) from the need to re-negotiate such Master Agreements or terminate existing transactions.

   As a starting point, we recommend that transactions in certain financial products, such as notional principal contracts, derivatives, securities lending and sale/repurchase (repos), ***where the financial products clearly do not have U.S. referenced assets***, be excluded from the passthru payment provisions.

3. If payments generally under a Master Agreement remain in the scope of the passthru payment provisions, and thus can be considered passthru payments:

   a. PFFIs should be entitled to transact under pre-2013 Master Agreements for a two-year period (***until July 1, 2015***) while the PFFI renegotiates its Master Agreement to update them with the necessary FATCA withholding tax provisions. During this two-year grace period, no withholding should apply to payments made pursuant to the Master Agreement, regardless of whether the counterparty opens a new account or otherwise provides documentation to the PFFI during this time frame.

   b. Given the volume of new regulatory requirements within the industry affecting capital markets products (e.g. G20, Dodd-Frank, Volcker) which may require further changes relating to the clearing and settlement of capital markets financial products, and other requirements to restructure large portions of the capital markets sector, a further two-year grace period should be provided (***to July 1, 2017***) to allow PFFIs time to

coordinate and build any withholding systems that are found to be necessary.

Background

The capital markets businesses of our member firms have thousands of negotiated contracts (for ease of consideration, collectively referred to in this letter as "Master Agreements") with a variety of counterparties, many of which will need to be re-negotiated in light of FATCA – provided that the counterparties to these contracts are willing to enter into re-negotiations. Re-negotiation of these contracts will be required primarily for two reasons:

i. If payments made under existing contractual arrangements are treated as passthru payments, terms of the contracts may need to be renegotiated. If a counterparty to a PFFI's contract chooses to be a non-participating FFI (NPFFI) or is a recalcitrant account holder, the PFFI may be required to gross-up the payments under existing contracts for any passthru payment withholding. This would seem to run counter to the intent of FATCA, essentially placing the burden of FATCA non-compliance with the PFFI instead of the NPFFI/recalcitrant account holder.

ii. Accounts that are created pursuant to negotiated bi-lateral or multi-lateral Master Agreements are not subjected to the standardized account opening process and documentation used for other types of accounts, and any changes to the account must be negotiated on a contract-by-contract basis (and not by a mailing to advise the account holders that the standard terms have changed). Many standard Master Agreements executed by FFIs do not contain a requirement for a counterparty to provide U.S. tax documentation. In order to obtain U.S. tax documentation, a PFFI would have to open up negotiations – and where the contract contains gross-up provisions, there will be little incentive for a NPFFI to cooperate (because as stated earlier, the cost of non-compliance will be borne by the PFFI).

PFFIs may seek to terminate transactions rather than bear the burden of the FATCA withholding implications; however, the termination of Master Agreements presents its own particular difficulties and repercussions. Termination may result in potential legal action and damages; it may also necessitate the termination of offsetting hedge transactions with other counterparties, incurring further costs and instability in the capital markets as a whole.

We note that given the current lack of symmetry between the application of FATCA to FFIs (who are subject to the passthru payment provisions) and USFIs (who are not

subject to the passthru payment provisions), PFFIs face a far greater economic burden and business risk than their U.S. counterparts, as PFFIs are at risk of needing to terminate a considerable number of contracts, while their U.S. competitors would need to terminate relatively few contracts. Moreover, if this asymmetry continues to exist post-March 18, 2012, non-compliant counterparties may transfer their future business to USFIs to avoid FATCA withholding and disclosure to the IRS.

Urgency

If the passthru payment provisions of FATCA apply to Master Agreements, PFFIs with capital markets businesses will be forced to re-open negotiations with counterparties with respect to existing Master Agreements (in particular, those executed after March 18, 2010, the unilateral termination of which may expose the terminating party to to penalties and/or legal disputes), and to develop withholding systems related to payments made pursuant to Master Agreements. All of the Master Agreements that do not contain FATCA provisions will need to be renegotiated or PFFIs will be economically motivated to cease or dramatically restrict the transactions they will enter into with a number of counterparties after March 18, 2012. Amending thousands of Master Agreements will take a considerable amount of time and resources.

While the grandfathering relief in the FATCA legislation is applicable to both withholdable and passthru payments on fixed term obligations entered into on or before March 18, 2012, this provides only a very small window of time after the anticipated release of draft regulations (end of 2011) for renegotiating contracts where transactions will be confirmed after the grandfathering date.

We look forward to our opportunity to discuss these matters more fully. Please contact me if you have any questions.

Yours sincerely,

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Director
Investment Industry Association of Canada (IIAC)

Cc: Brian Ernewein, General Director, Assistant Deputy Minister's Office, Tax Policy Branch, Canadian Department of Finance

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