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RE : Foreign Account Tax Compliance Act Provisions in the Hiring Incentives to Restore Employment Act of 2010 ("FATCA")

Dear Messrs. Eggert and Grinberg;

Royal Bank of Canada and its subsidiaries ("RBC") are pleased to have the opportunity to meet with representatives from the U.S. Treasury and Internal Revenue Service ("IRS") on July 7th to provide our initial comments on the impact of the FATCA provisions, and to provide input on the regulations and guidance that will be required to implement same.

RBC is a multinational organization, offering a diverse range of financial services to clients worldwide, as we will discuss in more detail below. Although we are still in the early stages of assessing the impact of FATCA on our business, it is clear that the implications are far-reaching and complex. We appreciate that Treasury and the IRS face a significant challenge to develop detailed regulations and guidance within a very short time period and we hope that we are able to provide practical information and input as you work to develop detailed requirements that satisfy the compliance objectives of FATCA, without placing a disproportionate burden upon foreign financial institutions ("FFIs").

As indicated, we are still in the early stages of assessing the impact of FATCA to our current business and our future strategic plans, and therefore, our comments are

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preliminary. However, our hope is to provide you with some written comments prior to our meeting to provide a sense of the scope and magnitude of our concerns. Given our ongoing review assessment of FATCA's implications for RBC, these comments are by no means exhaustive. In that connection, we are prepared to provide additional comments when we meet on July 7th or following the meeting. We also understand that Treasury and the IRS intend to issue preliminary guidance in proposed form in the near term. We anticipate that we will have further comments in response to the proposed guidance and we would be pleased to provide further input in connection with any specific requests in that guidance.

Overview

We have organized our comments as follows:

1. RBC – Background Information
2. Ke y Issues and Preliminary Recommendations
    a. Exclusions from the Definition of United States Accounts
    b. Issues Related to Specific Businesses and Account Types
    c. Comments Related to Requirements under the FFI Agreement that have General Application

1) RBC – Background Information

Royal Bank of Canada and its subsidiaries operate under the master brand name RBC. RBC is Canada's largest bank as measured by assets and market capitalization, and is among the largest banks in the world based on market capitalization. RBC is one of North America's leading diversified financial services companies, and provides personal and commercial banking, wealth management services, insurance, corporate and investment banking and transaction processing services on a global basis. RBC employs approximately 77,000 full- and part-time employees who serve more than 18 million personal, business, public sector and institutional clients through offices in Canada, the U.S. and 52 other countries. Approximately 75% of the clients are serviced through offices in Canada, 18% through offices in the U.S. and the remaining 7% through other countries.

RBC operates under five major business lines:

- Canadian banking;
- Wealth management, which includes discount and full service brokerage, trustee services (personal trusts, funds, employer-sponsored plans, etc.), estate administration, investment management, custody, and retail mutual funds;
- International banking;
- Insurance, which includes property, auto, travel, disability and critical illness, term life, universal life, deferred and life annuities, and segregated funds; and
- Capital markets.

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Clients are divided by business line approximately as follows:

- Canadian banking – 61%
- Insurance – 22%
- Wealth management – 5%
- International banking – 12%
- Capital markets - < 1%

There are currently 12 RBC entities located in 7 different countries that have active Qualified Intermediary ("QI") Agreements in place with the IRS. Approximately 263,000 accounts received U.S. source reportable amounts under these QI Agreements in 2009. As such, this represents only a very small portion of RBC's overall client base, whereas entering into an agreement as provided under FATCA (an "FFI Agreement") will potentially impact more than 18 million clients.

Other details which are indicative of the scope and magnitude of the impact include the following initial estimates:

- Number of RBC FFIs that could potentially enter into FFI Agreements with the IRS – > 70
- Number of products offered by RBC (many of which have separate account opening documents that could require amendments to comply with the FATCA provisions) – >2,000
- Number of significant IT systems that could require changes in order to comply with the FATCA provisions – > 70

Clearly, our current businesses will be affected by the provisions under FATCA. In addition, we believe it is relevant and important to point out that the implications of FATCA will inform and influence our future product development, business activities and investments.

2) Key Issues and Preliminary Recommendations –

a) Exclusions from the Definition of "United States Account"

The legislation provides Treasury with significant powers to prescribe the detailed regulations and guidance necessary and appropriate to implement the FATCA provisions. We respectfully encourage Treasury to use these powers in a manner that meets the objectives of the legislation without placing a disproportionate burden upon FFIs entering into FFI Agreements ("participating FFIs"),. As outlined below, we believe that the potential burden can be significantly alleviated without compromising the objectives of the legislation by prescribing exclusions, for both new and existing accounts, from the definition of "United States account".

i. Exclusion for foreign entities exempt from withholding under section 1472(b)

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Under section 1471, certain payments to an FFI are subject to withholding unless the FFI has agreed to comply with information reporting requirements in connection with its United States accounts. For this purpose, United States accounts are those held by specified U.S. persons or foreign entities with substantial U.S. owners.

Under section 1472, certain payments to a non-financial foreign entity ("NFFE") are subject to withholding unless information is reported regarding the identity of any substantial U.S. owners of the foreign entity or a certification is made that the entity does not have any substantial U.S. owners. However, section 1472(c) provides an exemption from the withholding and reporting requirements for the following types of foreign entities:

- Non-U.S. corporations whose stock is regularly traded on an established securities market, and any corporations which are members of the same expanded affiliated group;
- Any entity which is organized under the laws of a possession of the U.S. and which is wholly owned by one or more bona fide residents of such possession;
- Any foreign government, any political subdivision of a foreign government, or any wholly owned agency or instrumentality of any one or more of the foregoing;
- Any international organization or any wholly owned agency or instrumentality thereof;
- Any foreign central bank of issue; and
- Any other class of persons identified by Treasury.

The Joint Committee on Taxation ("JCT") Technical Explanation to the FATCA provisions indicates that it is expected that coordinating rules will be provided for the application of the provisions applicable to FFIs and the provisions applicable to foreign entities that are NFFEs.

We submit that guidance is necessary to clarify that the exceptions provided under the NFFE withholding and reporting rules of section 1472 also apply for purposes of the FFI withholding and reporting rules of section 1471. To ensure consistency of application, accounts that are excepted under section 1472(c) should also be excluded from the definition of "United States account" under the terms of the FFI Agreement, and the FFI therefore should not be required to determine whether the NFFE has substantial U.S. owners or to report on any such owners. To this end, we suggest that the regulations or guidance ensure that accounts for account holders that are NFFEs, and which fall within one of the enumerated exceptions in section 1472(c), are carved-out from the definition of "United States account" for purposes of the withholding and reporting rules applicable to FFIs.

ii. Exclusion for Canadian entities exempt from withholding under Article XXI of the Canada-U.S. Income Tax Treaty

The information reporting rules of section 1471 apply to United States accounts of an FFI, which are accounts of specified U.S. persons or foreign entities with substantial U.S.

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owners. Under section 1473(3), the definition of specified person excludes "any organization that is exempt from tax under section 501(a) or any individual retirement plan." Therefore, no reporting is required with respect to accounts of these U.S. tax-exempt entities.

The Canada-U.S. income tax treaty includes rules effectively providing mutual recognition of certain tax-exempt entities in the two countries. Under Article XXI of the treaty, income of religious, scientific, literary, educational or charitable organizations exempt from tax in Canada is exempt from U.S. tax provided that such income is not from carrying on a trade or business. Article XXI similarly exempts from U.S. tax dividend and interest income derived by a trust, company, organization or other arrangement that is generally exempt from tax in Canada and that is operated exclusively to administer or provide pension, retirement or employee benefits. Thus, the Canada-U.S. tax treaty provides a U.S. tax exemption for entities that are comparable to the U.S. entities that are excluded from the definition of "United States account".

In that connection, we suggest that the relevant guidance provide an exclusion from the definition of "United States account" for those Canadian entities that are covered by Article XXI of the Canada-U.S. tax treaty. Without such an exclusion, these entities would trigger reporting obligations under the FATCA provisions that would not be applicable to comparable U.S. entities. Practically speaking, this would give rise to more onerous reporting obligations in connection with the accounts of such Canadian entities when compared to those that are organized in the U.S. As such, it would seem appropriate that accounts of Canadian registered pension plans, RRSPs, RRIFs, charities and not for profits, educational and religious institutions that are exempt from tax in Canada and exempt from U.S. tax under Article XXI of the Canada-U.S. tax treaty should be excluded from the definition of "United States account" for purposes of the withholding and information reporting rules of section 1471.

iii. Exclusion for other Canadian account types that represent a low risk of tax evasion

Under the Income Tax Act (Canada) (the "ITA"), there are a number of provisions which permit Canadian taxpayers to open accounts under special types of plans with financial institutions that are registered with the Canada Revenue Agency ("CRA") and are designed to provide certain tax advantages in specific circumstances, including general personal savings ("Tax Free Savings Accounts" or "TFSAs"), saving for education ("Registered Education Savings Plans or "RESPs"), and assistance to disabled individuals ("Registered Disability Savings Plans" or "RDSPs").

Depending on the type of plan, tax advantages may be provided to planholders in a variety of ways. For example:

- contributions to the plan might not be tax-deductible, but income and gains earned within the plan are tax-exempt, or tax-deferred until withdrawn.

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- contributions to the plan might be tax-deductible, and income and gains earned within the plan are tax-deferred while remaining in the plan, but are fully taxed when withdrawn.

To limit the amount of tax benefits provided by these types of arrangements, the ITA sets out numerous conditions that must be satisfied. Examples include the following.

- The plans must be registered with the CRA and the plan administrator must report certain information to the CRA (e.g., contributions and withdrawals).
- Annual or aggregate contributions to the plan are generally limited and excess contributions are subject to penalties until withdrawn.
- The life of the plan may be restricted.
- The plan may require eligible planholders or beneficiaries to satisfy certain restrictions (e.g., mental or physical disabilities, attendance at qualified educational institutions, etc.)
- The use of the funds accumulated in the plan may be limited to certain purposes in order to qualify for beneficial tax treatment.

Given the restrictions attached to these types of plans and the manner in which they are closely monitored by the CRA, we recommend that such arrangements be excluded from the definition of "United States account" on the basis that they present a low risk of being used by U.S. persons for tax evasion.

We also recommend that delivery against payment ("DAP") accounts with broker dealers (also known by such other names as "cash on delivery", "delivery versus payment", etc.) be excluded on the basis that the broker dealer is simply the intermediary that is executing trades on behalf of the beneficial owner, and such transactions are also reported by a financial institution ("FI") that maintains a custodial account for the beneficial owner. As all transactions processed by the executing broker are also reported by the FFI that maintains the custodial account, we suggest that the reporting by the executing broker would be duplicative. In addition, if an FFI that maintains the custodial account is not a participating FFI, all withholdable payments made to the non-participating FFI for the benefit of the account holder would be subjected to 30% withholding. Therefore, we propose that DAP accounts be excluded on the basis that reporting would be duplicative and that the other reporting with respect to these types of accounts ensure that they present a low risk of being used by U.S. persons for tax evasion.

iv. Exclusion for deposit accounts with an aggregate value <$50,000

FATCA provides an exception from the definition of "United States account" for depository accounts maintained by an FFI where the aggregate value of the depository accounts held in whole or part by an individual does not exceed $50,000. The Secretary is given authority to provide rules treating all members of the same expanded affiliated group as a single financial institution for purposes of measuring the $50,000 threshold.

We respectfully encourage the Secretary to limit the exercise of its discretion to require such aggregation of separate entities. As earlier submissions from other interested

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parties have indicated, incompatible or dissimilar IT systems maintained across an affiliated group, in addition to the legal restrictions related to the sharing of information between legal entities without consent, would create significant difficulties for (or effectively prevent) many FFIs from applying this $50,000 threshold in its current form. Without some indication that this aggregation of accounts will be required only in limited circumstances (e.g., those involving some evidence of potential abuse), FFIs may not be able to make the investment in the IT systems changes necessary to measure and monitor whether aggregated accounts for a particular client are below the $50,000 threshold. Practically speaking, this would make the exception for smaller accounts unavailable.

We also request that some consideration be given to permitting the $50,000 threshold to be measured at specific points in time rather than continuously. Measuring on this basis should produce a substantially similar result as would measuring on an ongoing basis. Conversely, it would be extremely costly to make the necessary systems changes to monitor the dollar amount thresholds on a continuous ongoing basis, particularly when most deposit accounts will likely be in a foreign currency and therefore require conversion into U.S. dollars.

Also in connection with the threshold issue, the legislation provides that the exception for accounts under the $50,000 threshold applies automatically unless the FFI elects to have the provision not apply. We suggest that no formal filing or statement be required by an FFI to make such an election. If accounts below this level are reported, such action should be accepted as an election not to apply the threshold provision.

We would also suggest the regulations or guidance provide a clear definition of a "depository account" and confirm that such an account does not include a fixed income certificate, guaranteed investment certificate (the Canadian equivalent of a Certificate of Deposit ("CD" in the U.S.)), term deposit and other such investment.

v. Exclusion for other types of account holders that represent a low risk of tax evasion

There are a number of other types of account holders (Canadian and non-Canadian) that we have identified as posing a low risk of tax evasion and we submit should therefore be excluded from the definition of "United States account". We intend to provide additional written comments in support of such exclusions to you in a separate letter to follow; however, the following are some examples of categories of account holders for which we believe further exclusions will be appropriate:

- Residents of a jurisdiction for whom income and/or other transactions are reported by the FFI to the tax authority of that jurisdiction, particularly in the case of a jurisdiction that subjects its residents to tax rates on such amounts that would make the use of the account for tax evasion unlikely. For example, there is reporting of income earned in excess of a nominal threshold ($50) on bank balances or through a securities account for Canadian residents to the CRA. Other jurisdictions may have similar requirements.
- Religious, charitable, non-profit and educational organizations.

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- Employer-sponsored plans and arrangements, including pension plans, employee-stock savings plans, etc.

b) Issue s Related to Specific Businesses and Account Types

As indicated earlier in this letter, RBC provides a full range of financial services and products to its clients. In this section, we will discuss some issues, concerns and recommendations related to specific types of businesses and accounts.

i. Trusts

The application of FATCA to trust companies and personal trusts (i.e., trusts settle by and for the benefit of private individuals as opposed to commercial trusts or collective investment vehicles, an interest in which is typically defined by reference to units, which a beneficiary (or investor) acquires for consideration) is an area of concern to RBC. A number of RBC entities in several jurisdictions act in a fiduciary capacity as trustee of such personal trusts. In addition, the majority of RBC FFIs have accounts for entities that are trusts. These trusts may have corporate or personal trustees. In that connection, we submit that the regulations and guidance should clearly define the application of the FATCA rules to various types of trusts and trust arrangements.

The issues related to trusts are complicated and cannot be fully addressed in this document or during our initial meeting on July 7th. However, we have identified our initial key concerns and recommendations below, and we would welcome the opportunity to work closely with Treasury and the IRS to ensure that the detailed requirements minimize uncertainty and address the operational and administrative challenges related to these types of arrangements.

1. Trust Companies as FFIs versus Trusts as NFFEs

FATCA defines a "financial institution" to include any entity that, "as a substantial portion of its business, holds financial assets for the account of others". While it could be argued that a corporate trustee holds financial assets for the benefit of beneficiaries of a trust, we recommend that a distinction be made between trust companies that retain custody of trust assets (i.e., effectively providing both trustee and custodial services) and trust companies that open financial accounts with other FFIs which hold custody of trust assets (i.e., providing trustee, but not custody services).

In the first situation, the trust company will have robust custodial recordkeeping and reporting systems, and generally have the capabilities to make the changes necessary to comply with the terms of an FFI Agreement. In the second situation, the trust company may not have robust electronic recordkeeping systems, especially with respect to the recording and reporting of transactional data, as they have not had the need for such systems in order to fulfill their fiduciary responsibilities. Instead, they may rely on the

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recordkeeping and reporting services provided by the financial institutions where they maintain financial accounts.

In the case of a trust company that opens financial accounts for trusts with other FIs (i.e., "holding FIs"), we propose that the final regulations and guidance provide flexibility to allow the trust company to have the holding FI treat the account as an account for the trust company as an FFI, or to treat the account as an account for an NFFE (i.e., the trust). In the first situation, the trust company will be responsible for the identification and reporting of any trusts that are United States owned foreign entities. In the second situation, the trust company will either provide the holding FI with a certification that the trust does not have any substantial United States owners, or will provide the name, address and TIN of each substantial United States owner of the trust.

2. Identification of "substantial United States owners" of a Trust

In the case of trusts that are not collective investment vehicles, FATCA generally defines a "substantial United States owner" to be any specified United States person:

- treated as an owner of any portion of the trust under the U.S. grantor trust rules, and
- to the extent provided by the Secretary in regulations or other guidance, who holds, directly or indirectly, more than 10 percent of the beneficial interests in the trust.

Unless the regulations and guidance provide greater clarity regarding the identification of substantial United States owners of a trust, we anticipate that making this determination will create significant on-going problems, including client frustration and dissatisfaction, administrative costs related to the additional time that will be spent on such accounts, and frequent uncertainty as to whether the rules have been applied correctly. Given that the majority of these accounts are unlikely to be United States accounts, it is our view that the burden on the FFI will significantly outweigh any benefit derived by the IRS.

In that connection, we are familiar with the difficulties that can arise as a result of to applying complex U.S. tax rules to non-U.S. entities in an effort to determine the type of documentation that is required under QI Agreements. Given that the number of accounts that will likely be affected by FATCA is far greater than the relatively small number that currently operate under QI Agreements, it is our sincere hope that such uncertainty can be addressed for participating FFIs under the proposed FATCA regime. In that connection, it should also be noted that these difficulties will likely be even more pronounced for the non-corporate trustees of trusts for which RBC has financial accounts. Many of these trusts are small and have non-professional trustees.

We submit that non-U.S. trustees should not be expected to engage U.S. tax advisors to advise on the application of these complex U.S. definitions to their trusts. Similarly, the employees of FFIs should not be expected to assist clients in the interpretation of the U.S. trust provisions.

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Issues of particular concern include the following:

- Identification of an owner under the complex grantor trust rules. We are concerned that the far-reaching definition could result in a non-U.S. inter-vivos trust inadvertently having a U.S. owner as a result in a change of residence of a contributor or beneficiary of the trust.
- Identification of persons with a beneficial interest in a non-grantor trust. We propose that such persons be limited to those beneficiaries having a current vested entitlement to revenue and/or capital from the trust.
- Measurement of a person's beneficial interest in a non-grantor trust. Although this may be simpler to measure in the case of a non-discretionary trust, there is still uncertainty as to how to measure against the 10% threshold when some beneficiaries' entitlements may be limited to a fixed share of only the revenue or only the capital of the trust. In the case of a discretionary trust, the basis for measurement is even less clear. Given that a discretionary beneficiary has no actual entitlement until the trustee takes the necessary steps to exercise its discretion in favour of the beneficiary, it could be argued that in the case of a discretionary trust, no beneficiary has a beneficial interest in excess of 10%.

  Similar issues would exist under U.S. tax rules that require a U.S. person to report certain interests in passive foreign investment companies ("PFICs"). We understand that there is little or no guidance regarding the attribution of stock ownership in a PFIC to a beneficiary of a fully discretionary trust. We also understand that the IRS considered this in a private letter ruling, in which it suggested that patterns of distributions and mortality tables based on the age of each beneficiary could be analyzed to determine the actuarial interest of a beneficiary.

  Equally, in the case of trusts where the distribution of capital is contingent on a future event (such as the death of the revenue beneficiary), the individuals entitled to the capital, and their respective share, cannot be determined definitively until that future event occurs.

  We suggest that it would be very difficult for non-U.S. trustees to correctly interpret, analyze and apply these rules.

3. Privacy and Other Regulatory Concerns

In the case of a trust (or other NFFE) that is determined to be a United States owned foreign entity, it is not only the information relating to the United States substantial owner that is being reported to the IRS, but also the information relating to the entity itself. We have not yet had an opportunity to consider the more complex issues that may arise in this situation as a function of the varied and robust privacy and confidentiality laws which govern our operations.

4. Requirement to Close a United States Account

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Under the terms of the FFI Agreement, a participating FFI may be required to close a United States account that does not provide a waiver of a foreign law that would otherwise prevent the reporting of required information related to the account to the IRS. Although it may be possible for an FFI that has a United States account for a trust to close the financial account, it seems less likely that a participating FFI that is trustee can simply "close" or "terminate" the trust. Being a fiduciary relationship (as opposed to a contractual account), the FFI trustee faced with this position might have two options: (i) retire as trustee in favour of another trustee that is likely to be faced with the same issue and therefore may be difficult to find; or (ii) appoint the assets to a beneficiary, thereby terminating the trust. Any such fiduciary decisions not taken in the best interests of the beneficiary could leave the trustee exposed to a breach of trust claim. This issue is being considered further.

5. Inter Vivos Trusts versus Testamentary Trusts and Estates

Given our understanding of the policy reasons behind the FATCA legislation, we propose that consideration be given to limiting the application of FATCA to *inter vivos* trusts (i.e., trusts created during the lifetime of the settlor), and exempting estates and testamentary trusts (i.e., trusts arising under the will of an individual following their death). In our Canadian trust business, where RBC acts as corporate executor and trustee, the majority of the accounts are estates or testamentary trusts. Canadian anti-money laundering legislation and regulation also reflects the policy difference between *inter vivos* and testamentary trusteeships and has tailored the collection of information and reporting requirements accordingly. We propose that estates and testamentary trusts be excluded on the basis of presenting a low risk of being used by U.S. persons for tax evasion.

ii. Investment Funds

We understand that a number of groups representing the fund industries in several jurisdictions (including the European Fund and Asset Management Association ("EFAMA") and the Investment Funds Institute of Canada ("IFIC")) have provided or will be providing comments and recommendations to Treasury and the IRS with regards to the application of FATCA to investment funds. As such, we will limit the comments in this letter to those that we see as particularly significant to RBC.

RBC will be impacted from a number of perspectives by the requirements contained in the final FATCA regulations and guidance as they may apply to funds (and other collective investment vehicles ("CIVs")) and their investors. In addition to offering a wide-range of RBC-managed mutual and pooled funds in Canada, Jersey, Guernsey and Switzerland, RBC offers a variety of services to funds and their investors. For example:

- RBC and third party Canadian retail funds can be purchased, sold and held by clients through accounts opened and maintained with RBC's Canadian bank branches.
- RBC and third party funds can also be purchased, sold and held by clients through accounts opened and maintained with RBC's broker/dealers and several RBC entities that offer custodial services.

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- RBC provides a variety of services to the funds themselves, including investment management, trusteeship, custody, fund accounting, net asset valuation, and unitholder recordkeeping. It is important to note that it is not unusual for RBC to provide only some of these services to a fund. A fund may engage separate service providers for different fund-related activities.

The manner in which the units of many funds are distributed, registered and held creates significant practical operational challenges that would make it very difficult (if not impossible) for most funds to comply with the requirements of an FFI Agreement as an FFI. The funds themselves may have very little information about the unitholders of the funds if units of the funds are distributed through other intermediaries or even a chain of intermediaries. This makes it operationally difficult for the fund to be responsible for the identification and reporting of any United States accounts.

Another aspect of FATCA (as it might apply to funds) that concerns RBC relates to any potential requirement to withhold on passthru payments made to recalcitrant account holders. It is difficult to see how this could practically be implemented in the case of funds (or other CIVs). Some of the challenges include the following:

- Determining at what point withholding should be applied (e.g., when a withholdable payment is made to the fund, when a distribution is made from the fund to an investor, etc.).
- Identifying recalcitrant accountholders subject to withholding on any passthru payment where the entity that is identified as responsible for withholding is not the entity that identifies recalcitrant accountholders. This requires that information be communicated between intermediaries, or potentially through a chain of intermediaries. This would be an extremely burdensome process which would likely need to be performed manually.
- Measuring the portion of a payment made to a recalcitrant account holder that would be considered to be a passthru payment subject to withholding and applying the tax. Given that a unitholder of a fund does not generally have a dividend interest in any of the assets of the fund and, in many funds, investors change on a frequent basis, it is unclear how this amount would be calculated. This would seem to be particularly true in the case of proceeds, given that funds generally only allocate net capital gains to unitholders. Any effort to allocate proceeds would be a potentially greater challenge. In Canada, most funds only make capital gains distributions to investors holding units at the end of the taxation year.

Given that the vast majority of fund units are held in accounts with other FFIs that may be participating FFIs which would be taking steps to identify United States accounts and to report such accounts to the IRS, we submit the following for consideration:

- Exclude funds from the definition of "financial institution", in which case the FATCA provisions applicable to NFFEs would apply. Funds or groups of funds that have the ability to comply with the terms of an FFI agreement could be given the option to elect FFI treatment.

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- Provide an exclusion from the definition of "United States account" for funds that are widely-held. (We understand that several interested parties have suggested that "widely-held" should be defined to include funds with more than 100 investors, and we support this recommendation.) Given that most funds will likely be held in accounts with participating FFIs, it is likely that investors in such funds will be identified and reported by such FFIs. To also impose reporting requirements on the fund would result in duplicative reporting.
- As a general rule, exempt any portion of a U.S. source payment made to a fund with recalcitrant account holders, as well as any payment made to a recalcitrant account holder receiving a distribution from a fund that receives U.S. source income and proceeds, from Chapter 4 withholding. As a minimum, we suggest that any such withholding requirements be suspended during an appropriate transition period in order to allow time to address any recalcitrant account holder situations. We anticipate that most participating FFIs will have very few recalcitrant accounts among new accounts opened on or after the effective date for the new requirements. If it is felt that there are situations where there is the potential of abuse, the more immediate application of the withholding requirements should be directed to those situations (e.g., funds that have a significant percentage of units held by recalcitrant accounts holders).

iii. Insurance

RBC is a member of the Canadian Life and Health Insurance Association Inc. ("CLHIA"), which is a voluntary association of Canadian life and health insurers. Its members account for over 99% of Canada's life and health insurance business.

The CLHIA submitted its comments related to the potential impact of FATCA to Canadian life insurance companies in a letter to Treasury dated June 15, 2010. (See copy enclosed.) RBC endorses the comments and recommendations of the CLHIA. Therefore in this section, we have limited our discussion to a few of points that are of particular interest to RBC.

1. Insurance products subject to FATCA

As indicated in the first section of this letter, RBC's Insurance business offers a full range of insurance products. We suspect that it is not the intention of Treasury to have FATCA apply to policies which are designed to provide pure insurance protection with respect to specific risks and which clearly have no client investment component (e.g., property, auto, travel, term, disability and critical illness insurance among others). For RBC, these types of policies represent almost 90% of our accounts.

The Joint Committee on Taxation ("JCT") Technical Explanation of FATCA indicates that it anticipates that the Secretary may prescribe that certain contracts or policies, "for example annuity contracts or cash value life insurance contracts" are financial accounts.

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For purposes of analyzing the impact of FATCA on RBC, it would be helpful if Treasury and the IRS were to clarify the types of insurance products (if any) that are subject to FATCA.

2. Exclusions for Certain Canadian Insurance Companies or Insurance Accounts

As discussed in the CHLIA letter, there are strong arguments to support the exemption of many or most Canadian insurance companies from FATCA, including the following:

- Most Canadian life insurers do not sell their products to non-residents because of anti-money laundering and anti-terrorism legislation, as well as underwriting policies.
- Canadian tax legislation strongly discourages Canadian life insurers from issuing policies on the lives of non-residents.
- As discussed earlier, if a Canadian resident individual is also a U.S. person, given the Canadian personal tax system (including personal tax brackets and tax rates), there is likely to be little or no additional U.S. tax to be paid after claiming credits for taxes paid in Canada.
- The Canadian taxation of insurance products does not make them an attractive vehicle for tax evasion.
- It is our understanding that Canadian tax reporting slips issued to a U.S. resident will automatically be sent to the IRS by the CRA, pursuant to the exchange of information provisions of the Canada – U.S. tax treaty.

RBC's initial analysis found that based on current information, over 99.6% of clients with annuity contracts or life policies with cash values are residents of Canada, less than 0.4% of such clients are U.S. residents, and the percentage that are residents of other countries is negligible.

Given the arguments as to why Canadian insurance products that might be subject to FATCA are not attractive vehicles for tax evasion by U.S. persons and the high percentage of accounts that are for Canadian residents, we recommend that Treasury consider providing an exemption from the definition of "financial institutions" that would exclude a Canadian insurance company if substantially all policy holders are Canadian residents.

For those Canadian insurance companies that do not satisfy the requirement that substantially all policy holders are Canadian residents for purposes of the proposed exclusion, we would propose that the accounts held for Canadian residents qualify for exclusion.

iv. QI Entities

We understand that at some point in the future, Treasury will introduce changes to the QI Agreement to provide for the coordination of the provisions of Chapter 3 with the new provisions in Chapter 4. At that time, we suggest that consideration be given to amending the current definition of "reportable payments" contained in section 2.44 of the QI Agreement, to limit the Form 1099 reporting requirements of a non-U.S. payor QI to

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reportable amounts, as defined in section 2.43 of the Agreement. The current definition of "reportable payments" makes reference to the regulations that address where payments are made and where sales are effected. These rules are vague and difficult to apply, particularly with respect to non-U.S. source payments.

Given the additional expectations being placed upon QIs and their affiliates under FATCA, the additional information reporting that will be provided for United States accounts, and the authority given to the Secretary under the FFI Agreement to request additional information with respect to United States accounts, it seems unnecessary to retain the current reporting requirements as set out in the definition of reportable payments, particularly given that these requirements generally apply in only very limited situations.

Relieving QIs of Form 1099-B reporting requirements would also exclude them from the onerous cost basis reporting requirements that were recently enacted. Given the resources that QIs and their affiliates will expend to implement the FATCA requirements, we submit that it would be overly burdensome to also impose the cost basis reporting requirements upon them, particularly given the very small number of accounts that would be subject to the reporting obligations.

v. U.S. Branches of FFIs

We submit that the definition of "withholdable payment", for purposes of Section 1471, should be amended to exclude payments to a U.S. branch of a foreign bank.

In our view, it would be beneficial to limit the scope of the "withholdable payment" definition in the case of certain foreign entities that already have robust U.S. tax information reporting responsibilities, in order to reduce the potential for numerous additional FFI agreements and because there is a low risk of tax evasion. U.S. branches of foreign banks are treated as U.S. persons for most information withholding and reporting rules, and thus are required to fully comply with all U.S. information reporting and withholding laws and regulations. For example, U.S. branches of foreign banks must file IRS Forms 1099 with respect to payments to non-exempt recipients. In addition, they are subject to IRS audits. Consequently, they should be treated as U.S. withholding agents that are not FFIs for purposes of Sections 1471 and 1472.

In addition to the fact that they must already comply with U.S. laws, branches (and agencies) of foreign banks conduct extensive operations in the United States and engage in hundreds of millions of financial services and other transactions each year. Unless payments to such branches are treated as satisfying the FATCA requirements, each payor of a withholdable payment to such a branch would need to ensure that the bank has entered into an FFI agreement before making payments to the branch. Such a requirement would place U.S. branches of foreign banks at a competitive disadvantage compared to U.S. banks.

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This exclusion is contemplated in the JCT Technical Explanation of the FATCA provision wherein it states:

> "Additionally, the Secretary may identify classes of institutions that are deemed to meet the requirements of this provision if such institutions are subject to similar due diligence and reporting requirements under other provisions in the Code. Such institutions may include certain controlled foreign corporations owned by U.S. financial institutions *and certain U.S. branches of foreign financial institutions that are treated as U.S. payors under present law."*

c) Comments Related to Requirements under the FFI Agreement that have General Application

i. Identification of United States Accounts

1. Identification of existing United States accounts

The requirements under the final regulations or guidance related to the identification of United States accounts in existing client databases will likely be the single most significant variable cost factor when assessing the potential implementation costs associated with entering into FFI Agreements. Within our Canadian business, the vast majority of account holders are Canadian residents. It is important to note that the results of a 2006 Canadian census indicated that less than 1% of Canadian residents are U.S. citizens.

We are aware of comments submitted to Treasury and the IRS by other interested parties and fully support requirements that would focus on searching all potential fields in our electronic data bases to identify accounts with any indicia of U.S. connections and then take reasonable steps to obtain additional information in order to determine whether, in fact, the identified accounts are United States accounts. We submit that the cost of taking steps beyond searching existing fields in client databases will very likely impose additional costs on FFIs that are not only disproportionate to the number of additional U.S. accounts that could be identified, but may discourage some FFIs from entering into FFI Agreements.

We encourage Treasury and the IRS to develop regulations and guidance that reflect an appropriate balance between satisfying the objectives of FATCA and the costs of complying. The carve-outs discussed earlier in this letter will also be important for the purposes of achieving this balance.

In any case, we recommend that participating FFIs be granted a three-year transitional period to take any required action related to existing accounts and during this time, there should be no requirement to withhold on withholdable payments to such accounts.

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We would be pleased to provide additional information regarding any alternative approaches that Treasury and the IRS might be considering when we meet on July 7th, or following the meeting.

2. Methods for identifying United States accounts and exclusions

Section 1471(b)(1)(A) requires an FFI that enters into an FFI agreement to "obtain such information regarding each account holder of each account maintained by such institution as is necessary to determine which (if any) of such accounts are United States accounts".

Although FFIs may not currently gather the type of information that would allow them to determine which (if any) accounts are United States accounts, they do have procedures in place for purposes of gathering information regarding account holders, including for purposes of confirming the identity of account holders for anti-money laundering and anti-terrorism regulatory ("AML") purposes. We recommend FFIs be given the option of making modifications to existing procedures and documents in order to gather any further information required to identify United States accounts, rather than having to introduce additional procedures and documentation. This would include gathering information for specified United States persons and substantial United States owners (i.e., name, address, U.S. TIN). We believe that by integrating the new requirements into existing processes as much as possible, the cost and administrative burden placed upon participating FFIs will be minimized and, more importantly, within those FFIs with well-defined and automated processes, maximum levels of compliance will be achieved. Although some FFIs may still prefer to gather IRS Forms W-9 from United States accounts, such forms should not be mandatory if the FFI implements other procedures for gathering the information. Given that the information will be reported to the IRS on an annual basis in accordance with the terms of the FFI agreement, if there is an issue with the name, address or TIN of a U.S. person so reported, the IRS can request additional information from the FFI at a later date.

With respect to the types of exclusions recommended in Section A above, there should be flexibility to allow the FFI to employ reasonable methods to determine whether or not an entity is one that qualifies for exclusion - for example, reliance on name where widely known (e.g., University of Toronto), information gathered from documents in the possession of the FFI (e.g., constating documents that identify the nature and purpose of the entity), information gathered from public websites, etc. The FFI should also be able to rely on information-gathering methods that are acceptable for AML purposes.

Circumstances in which the FFI is required to obtain IRS Forms W-8 should be limited to those where there are U.S.-source withholdable payments flowing through the account unless the FFI gathers acceptable client due diligence documentation, as per the Attachment to their QI Agreement. This would be consistent with the stated use of the forms being to establish that a non-U.S. person receiving certain types of U.S. source payments is a foreign person, is the beneficial owner of the payment and if applicable, is a resident of a foreign country with which the U.S. has a tax treaty.

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For FFIs that choose to gather information using IRS Forms W-8, the Forms should be amended to incorporate the required additional information. Separate forms should be developed for different types of clients. The forms should also be made clearer and easier to complete by those intended to be completing the forms – i.e., non-U.S. persons who have no knowledge of U.S. tax laws. This has been a significant challenge for QIs, particularly in terms of defining entity types in accordance with U.S. tax rules. As discussed earlier, we are particularly concerned that when RBC opens accounts for trusts, trustees will expect RBC staff to provide information regarding the U.S. grantor trust rules for purposes of determining whether or not the trust has a U.S. owner, or how to determine a beneficiary's interest in a trust for the purpose of measuring the 10% threshold. It would be helpful if sufficient information was made available to foreign account holders to enable them to determine their particular status under FATCA. We submit that it is unreasonable to expect account holders to incur a cost to seek U.S. tax advice, particularly given that the majority of accounts will not be United States accounts.

In other situations, particularly with respect to accounts that do not receive any U.S.-source payments, obtaining Forms W-9 and/or W8 should be at the option of the FFI. In any case, the degree of precision currently required with respect to the completion of the forms should be addressed to ensure that forms do not inadvertently fail, resulting in accounts being viewed as recalcitrant even though the FFI has sufficient other information in its records.

Where a participating FFI makes reasonable efforts to determine whether an account is a United States account and is unable to obtain the necessary information, the account will be recalcitrant. Withholding at 30% will apply to U.S. source withholdable payments and passthru payments. If the account receives no U.S. source payments and has no U.S. indicia, no further action should be required by the FFI. We submit that the FFI should not be prohibited from opening, or be required to close, accounts for recalcitrant accounts holders where there are no U.S. indicia.

3. Validity of information gathered to identify United States accounts

In the case of accounts for individuals, including joint accounts, where the FFI has gathered information and determined that an account is not a United States account, the FFI should be permitted to continue to rely on that information indefinitely, until such time as it obtains information that suggests that the status of the account has changed (e.g., change of address). If an FFI initially obtains such information as place of birth, citizenship, etc., all of which indicate that the account is not a United States account, it seems unlikely that an individual would subsequently become a United States person, but not move to the United States.

Any requirements to renew information obtained from entities previously determined not to have any substantial United States owners must be carefully considered. This is potentially one of the most challenging and costly areas of ongoing compliance with the terms of the FFI Agreement. It is far more difficult to update information of this nature

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on an existing account than it is to obtain the information at the time of account opening. As such, the efforts required would likely be disproportionate to the number of additional United States accounts identified.

In the case of entities that are identified as being United States owned foreign entities and therefore subject to annual reporting to the IRS, we submit that there should be no need for the FFI to seek updated information, given that the account is already being reported and the IRS can use its authority under the FFI agreement to seek additional information. The FFI should be permitted to rely on the account holder to advise them of changes in ownership.

ii. Waivers for United States Accounts and Closing Accounts

Under the terms of an FFI Agreement, if there is any foreign law that would prevent the reporting of information with respect to any United States account, the financial institution is required to attempt to obtain a valid and effective waiver of such law from each holder of such account, and if such a waiver is not obtained within a reasonable period of time, to close the account.

As these provisions only apply to United States accounts, in the case of an account that is recalcitrant as a result of the FFI not being able to obtain sufficient information in order to determine whether or not the account is a United States account, the account should not be treated as a United States account, particularly where there are no U.S. indicia.

The implications of these requirements are complex and require further research into the relevant laws of several jurisdictions. We understand that various comments have already been submitted to Treasury and the IRS on this subject, including the fact that FFIs are entering into FFI agreements voluntarily and therefore may not be able to rely on provisions in the legislation of some jurisdictions which would otherwise permit the disclosure of information without consent if the such disclosure is for the purposes of complying with foreign laws.

Some of the other issues that we are still reviewing include the following:

- Obtaining waivers in the case of a United States owned foreign entity to permit the disclosure of information related to the entity.
- Obtaining waivers in the case of joint accounts where the account is set up in the name of all parties to the account, some of whom may not be U.S. persons.
- The inability to "close the account" in the case of an annuity contract, life insurance policy or a trust (where the FFI is also trustee).

We may have further comments on this issue at a later date.

iii. Withholdable and Passthru Payments

The definition of pass-thru payment should be clarified to apply only to limited situations where there is a reasonable concern steps are being taken to deliberately attempt to avoid

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withholding under Chapter 4 and there is a traceable link between the account holder and the withholdable payment. Interest paid on deposit accounts or short-term investment certificates by a non-U.S. bank should not be considered to include any portion that is a U.S. source withholdable payment or pass-thru payment.

Similarly, U.S. source payments (e.g., U.S.-source pension payments) deposited into a client bank account outside the U.S. should not be viewed as passthru payments subject to any withholding on the part of the receiving FFI if the account holder is recalcitrant. It should be the responsibility of the U.S. payor to determine the status of the beneficial owner of the payment, and withhold and report accordingly. The FFI is simply an agent receiving the payment on behalf of its account holder.

As a general rule, a portion of U.S. income or sales proceeds received by a foreign collective investment vehicle when distributed to an investor in a fund should not be defined to be a pass-thru payment. As was experienced with these types of payments under the QI Agreement, withholding on only a portion of a payment received or made creates significant operational challenges, and most often requires manual processing. For example, certain investment entities that are treated as flow-through entities for QI purposes (e.g., partnerships) make distributions throughout the year, but the allocation of the payment between U.S. source and non-U.S. source, and taxable or non-taxable is generally not available at the time of payment. Details of the composition of the payments are generally not available until after year-end, at which time QIs often rely on manual processes to make adjustments to refund excess tax withheld throughout the year and to effect required U.S. tax reporting. Considerable effort is often required to gather such information. Similar challenges occur with distributions from U.S. mutual funds where a portion of distributions made throughout the year includes a non-taxable return of capital. It is very difficult and costly to implement systems changes that allow withholding to be taken on only a portion of a payment, particularly because that portion is frequently not determinable at the time of distribution. Given that the number of accounts that will be subject to the terms of FFI Agreements will be significantly more numerous than those under QI Agreements, reliance on manual processes needs to be avoided. The administrative cost and risk of error will be too high for larger FFIs.

There are other instruments which also cause significant challenges for QIs, including instruments that may be issued by a non-U.S. entity, but are deemed to pay U.S.-source income for U.S. tax purposes (e.g., dual-source securities). We are seeing an increasing number of such instruments, particularly in Canada. Most QIs find it necessary to implement manual procedures to review such payments and make adjustments to take any additional U.S. withholding and to issue the appropriate reporting after year-end. It is also a challenge for QIs to identify such instruments when they are initially acquired. We anticipate that a very small portion of new accounts will be recalcitrant. As such, we suggest that payments on these types of instruments should be excluded from the definitions of withholdable and passthru payments.

iv. Reporting

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We are concerned that the reporting of financial information, particularly gross receipt and gross payments/withdrawals from an account may prove to be of limited value to the IRS and would at best only identify potential U.S. persons for further review. The information would not necessarily be indicative of amounts to be reported on a U.S. tax return.

Given that reporting of information based on transactional data is generally more complicated and costly from a systems perspective than reporting static data such as name, address and TIN, and account balance/value which is captured at a particular point in time, we recommend that the reporting of gross receipts and gross withdrawals/payments not be required as part of the annual filing, and that Treasury instead exercise its authority under the terms of the FFI Agreement to request the FFI to provide additional information with respect to any United States account.

We also suggest the benefit of reporting account balance/value be reconsidered to ensure that IRS will in fact be able to make effective use of the information to warrant the cost to FFIs of providing such information.

If Treasury and the IRS do conclude that the reporting of any financial information is necessary, we suggest a deferral of the effective date of such reporting be provided to reduce the strain that implementing the FATCA provision will place upon the Information Technology resources of FFIs.

We also suggest the following with respect to reporting –

- The default reporting period should be the calendar year.
- The filing deadline should be no sooner than June 30th following the year-end.
- There should be no requirement to send copies of the information reported to the IRS to the accountholder or substantial United States owner, although most FFIs would likely advise such persons that information regarding their account will be reported to the IRS.
- If FFIs are required to report account value/ balance:
  - The amount should be reported as at close of business on December 31.
  - The FFI should be permitted to report in the base currency of the account.
  - The method for determining account value should be based on existing procedures and practices. For example, if there are holdings in an account that an FFI does not currently value because of the difficulty of obtaining a current value, there should be no requirement to obtain a value for purposes of reporting under the FFI agreement.
- There may be other amounts and adjustments being posted to accounts that do not represent receipts or withdrawals/payments. For many FFIs, it may be difficult and costly to segregate such amounts from actual receipts, withdrawals and payments. Given the values will be of limited use in any case, we recommend that FFIs be permitted to simply report total debits and total credits to an account.
- Many FFIs that offer a variety of products will have accounts on a number of different systems. FFIs should be permitted to submit the required reporting information separately for each system. Similarly, if members of the same expanded

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affiliated group are covered under a single FFI agreement, each member should be permitted to submit their reporting separately. We submit that there should be no requirement for an FFI to aggregate their annual reporting to the IRS. Such a requirement would place an unnecessary financial and administrative burden upon FFIs, particularly in situations where filing is done electronically.

v. Audit Considerations

For large financial institutions with large numbers of clients, compliance will generally require highly automated procedures and processes. We recommend that the information that must be gathered to determine whether or not an account is a United States account be very clear, with no need for interpretation by the client or the employees of the FFI. Many products offered by FFIs are high volume and "low touch", and the client is often dealing with junior level staff who cannot be expected to understand or explain technical U.S. tax rules.

If the process is sufficiently integrated and imbedded into routine procedures, there is low risk of significant non-compliance if policies and procedures are being followed and subsequent systems changes do not alter processing logic.

For FFIs with large numbers of accounts and robust systems, we recommend that verification focus on actions taken by the FFI to implement policies, procedures and systems to achieve and maintain maximum compliance. Testing of actual accounts should be on an infrequent or exception basis.

We appreciate that developing detailed requirements and regulations related to audit procedures may not be a current priority. However, it is important for FFIs to have a reasonable understanding of the nature of the audit procedures that will apply if they enter into FFI agreements for purposes of assessing the cost and potential risks and exposure that may arise. In addition, as FFIs are making systems and procedural changes to comply with FFI Agreements, it would be beneficial if Treasury and the IRS could identify specific due diligence procedures that might facilitate the subsequent verification process.

In Closing

Because this letter contains business information, customer proprietary information and other information of a sensitive nature, we request that the Secretary treat this correspondence confidentially. If the Secretary believes that it is required to reveal the contents of this letter to the public pursuant to the Freedom of Information Act or any other law, please notify us as soon as possible. We will promptly provide additional information in support of our request for confidentiality with respect to the proprietary and business sensitive information.

Finally, we would again like to express our appreciation for the opportunity to meet with representatives of Treasury and the IRS on July 7th, 2010 to provide our initial comments

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related to FATCA. Please do not hesitate to contact the undersigned by phone at (416)955-3845 or e-mail at ann.noges@rbc.com with any questions regarding our written comments. We look forward to working with you as you develop the detailed regulations and guidance that will be critical to the implementation of the FATCA provisions.

Yours truly,

Ann Noges
Director, Taxation

Enclosure

cc: Manal Corwin, International Tax Counsel, U.S. Department of Treasury
Michael Danilack, Deputy Commissioner International, Internal Revenue Service
Steven Musher, Office of the Associate Chief Counsel International, Internal Revenue Service