



June 2, 2011

IRS Hunt for Tax Cheats Affects Canadian Banks

In its relentless pursuit of tax evaders who hide their assets in offshore bank accounts, the US government has come up with a new law called the Foreign Account Tax Compliance Act (FATCA) that was signed into effect last year by President Obama. Under this law, starting 2013 all foreign banks must report to the IRS all accounts held by US citizens and green card holders, including corporate accounts with significant US ownership, as well as what they own. Failure to comply will result in the IRS imposing a hefty 30% withholding tax on any US income, and transactions they or their customers do.

But when it comes to Canada, there is a big problem with compliance. This is due to the fact that Canadian banks do not require its account holders to declare their citizenship or immigration status. New accounts can be opened by anyone simply by proving identity using a driver's license and one other piece of identification. In addition, there are no checks on existing account holders.

Hence, Canadian banks do not know the citizenship of their customers and Canadian law does not compel them to find out.

This requirement has led to a flurry of protests. Canadian Bankers Association president Terry Campbell complained to the Canadian Finance Minister Jim Flaherty that US law "attempts to coerce foreign financial institutions into a reporting and withholding relationship with U.S. tax authorities." The Investment Funds Institute of

Canada is seeking exemption from this law for RRSPs and other registered plans as well as for accounts worth less than \$500,000. It is easy to imagine that without any concessions, the cost of regularly identifying US customers of all financial institutions in Canada would be astronomical. It is estimated that the cost could come up to a quarter of a billion dollars for each major financial institution. On the other hand, noncompliance would jeopardize the US operations of Canadian financial institutions.

The broader issue is one of trust, sovereignty and economic expedience. The US government already requires its citizens to declare all income from every source worldwide. Now the IRS is requiring foreign financial institutions to provide the same details on their American customers. This is obviously to enable the IRS to countercheck and match the two sources of information and identify discrepancies that would lead to tax evaders.

But the Canadian Revenue Agency (CRA) and the IRS already has extensive information sharing agreements and a complex tax treaty. Canadian financial institutions already report income paid to non-residents to the CRA. Therefore some quarters suggest that the more practical thing to do would be for the IRS to approach the CRA on a case-to-case basis when they have suspicions over certain accounts.