

QI Agreement

An update regarding the new QI Agreement

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Global Business Tax, FATCA

The IRS has released a new QI agreement by 31 July 2014 in Revenue Procedure 2014-39. We have set out below an overview of the main changes arising from the new QI agreement.

Summary of changes arising from the new QI agreement

1. General overview

On 29 June 2014 the IRS released Revenue Procedure 2014-39 (“Rev. Proc. 2014-39”) that contains the new Qualified Intermediary (“QI”) agreement. The primary purpose of the new agreement is to coordinate the Chapter 3 and Chapter 4 obligations for QI’s and hence much of Rev. Proc. 2014-39 focuses on coordinating the QI agreement with FATCA provisions, in particular around documentation, withholding and reporting obligations for QI’s.

Importantly, the new agreement permits both foreign financial institutions (“FFI’s”) and non-financial foreign entities (“NFFE’s”) to hold QI status going forward subject to meeting certain conditions. In the case of FFIs that have already obtained a GIIN for FATCA purposes, the new QI agreement is effective from 30 June 2014, or else the agreement is effective from the date the GIIN is issued. For NFFE’s acting on behalf of its shareholders or is a sponsoring entity, the new QI agreement is effective either from 30 June 2014 (where a GIIN was been obtained prior to that date) or the date the GIIN is issued. For NFFE’s that are not required to register for FATCA, and are renewing their QI agreement, the effective date is the later of 30 June 2014 (if its QI renewal is before that date), or the date of the IRS QI renewal notice (if not renewed before 30 June 2014). For any such NFFE’s that are first obtaining their QI status, the effective date is the date the QI-EIN is issued.

Any QI agreement in effect before 30 June 2014 expired on that date. Rev. Proc. 2014-39 supersedes the provisions of the QI agreement contained in Rev. Proc. 2000-12. As Rev. Proc. 2014-39 has removed the external audit procedures required under the previous QI agreement (discussed in section 2.6 below), Rev. Proc. 2002-55 that set out the audit procedures has also been revoked.

The new QI agreement expires on 31 December 2016 so it is aligned with the FFI agreement. A QI that submits an application for QI status before 31 July 2014 and is approved during 2014 may act as a QI from 1 January 2014 until 30 June 2014 in accordance with Rev. Proc. 2000-12.

Separately, new agreements covering obligations for withholding foreign partnerships and withholding foreign trusts are still to be released by the IRS.

2. Specific changes highlighted in the new QI agreement

There are various changes under Rev. Proc. 2014-39 and we have sought to highlight below the main impacts.

2.1 Status of QI's

QIs may be FFIs or NFFE's under FATCA. For FFI's, in order to maintain QI status, the FFI is required to satisfy the requirements and obligations of a participating FFI (including a reporting Model 2 FFI), registered deemed-compliant FFI (including a reporting Model 1 FFI and a non-reporting Model 2 FFI treated as a registered deemed-compliant), registered deemed-compliant Model 1 IGA FFI or, for a transitional period, a limited FFI. In addition, a certified deemed-compliant FFI (including a non-reporting IGA FFI) must assume the obligations of and be treated as a participating FFI, registered deemed-compliant FFI, or a registered deemed-compliant Model 1 IGA FFI with respect to all accounts it maintains.

For NFFE's, in order to maintain QI status, the NFFE is required to assume the obligations of a direct reporting NFFE under the US regulations (where it is a QI acting on behalf of its shareholders) or undertake certain other withholding and reporting obligations to the IRS (where the QI is acting on behalf of other persons).

2.2 Coordination of QI and FATCA obligations

An FFI that has entered into a QI agreement will be subject to the FATCA requirements for all accounts it maintains regardless of whether they are a QI designated account.

The QI agreement seeks to coordinate QI and FATCA reporting and withholding. Therefore to the extent to which a QI is required to file separate Forms 1042-S is partly dictated by whether the payments are ultimately being made to recalcitrant account holders, non-participating FFI's and certain US payees. In addition, reporting Model 1 IGA FFIs are not required to apply back up withholding and Form 1099 reporting provided the QI reports the account under FATCA, e.g., where US indicia are present, but the QI does not hold documentation to refute the indicia, it would be

expected to report the account to its local tax authority. In accordance with the Form 1042-S instructions, a QI that is an FFI is required to file all Forms 1042-S electronically from 2014 onwards.

The documentation requirements under the new QI agreement are similar to the previous provisions so that a QI (that is an FFI) can continue to rely on documentary evidence (as an alternative to Forms W-8) that is permitted under the QI's know your customer rules which are approved by the IRS. These requirements do not extend to a QI that is an NFFE which is required to obtain Forms W-8 and W-9 from its account holders.

The new agreement provides that Forms W-8BEN have a validity period generally of three full calendar years, consistent with the coordination regulations released by the IRS earlier in 2014. In certain circumstances, IRS forms provided by direct account holders of a QI that are not being used to claim treaty benefits may be valid indefinitely.

2.3 QI's acting as Qualified Securities Lenders ("QSL's")

The new QI agreement states that a QI acting as a QSL is required to act as a QSL with respect to all US source substitute dividends that it receives as either an intermediary or dealer. Therefore, in effect all transactions for which QSL status is assumed now fall within the scope of the QI agreement (including the new compliance procedures mentioned below). In addition, it is worth noting the revised Form W-8IMY envisages a QSL using this form going forward whether it is acting as intermediary or dealer.

2.4 Restricted use of Private Arrangement Intermediaries ("PAI's")

The new QI agreement provides that only a QI that is an FFI may enter into an agreement with a PAI. More interesting, as it currently stands, the PAI itself must be certified deemed-compliant FFI (other than a registered deemed-compliant Model 1 IGA FFI) which seems to severely restrict the use of PAI's going forward. In order to maintain PAI status, a PAI is also prevented from having direct account holders that are QI's, withholding foreign partnerships and trusts, participating FFI's, registered deemed-compliant FFI's or registered deemed-compliant Model 1 IGA FFI.

2.5 Continued use of joint account and agency options to document certain partnerships and trusts

Similar to the changes impacting PAI arrangements, the new QI agreement provides that non-withholding foreign partnerships and trusts that may qualify for these provisions are limited to certified deemed-compliant FFIs (excluding registered deemed-compliant Model 1 IGA FFI's), exempt beneficial owners and excepted NFFE's.

2.6 Compliance procedures

Perhaps the most substantial change introduced by the new QI agreement is the replacement of the external audit requirement with an internal compliance programme, consistent with FATCA. As a result the QI is required to designate a responsible officer to oversee compliance with the agreement and to make periodic certifications to the IRS. The agreement sets out the specific areas that are required to be covered by the certifications. The periodic certifications are required to be made every three years.

The compliance programme must include the following areas:

- Draft and update written policies and procedures to enable the QI to comply with its obligations.
- Provide training of said policies and procedures to all business lines that are responsible for reviewing documentation, withholding and reporting.
- Ensure systems and processes are in place covering the documentation of account holders and recording information required for reporting.
- Monitor business practices, as well as business changes such as acquisitions, that may impact the QI's compliance with the agreement.
- Designate an independent auditor to perform a periodic review of compliance; and
- make the periodic certifications to the IRS as required under the agreement.

The IRS is expected to provide additional guidance with respect to the scope of these procedures.

Please contact us, if you have any questions

We will, of course, be of assistance with a concrete evaluation or other questions on the QI agreement. If you are in doubt about the rules, you are most welcome to contact Richardt Tabori Kraft, tel. +45 2961 7393 or Anja Bechmann, tel. +45 4030 4112.