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# Operational Tax News

## QI Update - Final Qualified Intermediary Agreement released

**2 January 2017**

On 30 December 2016, the IRS released the final Qualified Intermediary Agreement (Final QIA) as part of the **Revenue Procedure 2017-15**. The Final QIA applies from 1 January 2017 but certain elements, in particular those related to the Qualified Derivatives Dealer (QDD) status, benefit from a phased-in implementation.

## Actions required

- A QI that seeks to renew its QIA must do so through the dedicated **online portal** before 31 March 2017. In that case, the QIA will be considered to be effective as of 1 January 2017. A **user guide** is available to assist QIs with the creation and management of their online account. It is worth noting that the QI portal is separate from the FATCA portal.

- QIs must implement a QI compliance program that includes policies, procedures, and trainings relevant for complying with QI obligations under the QIA. As part of the compliance program, the QI responsible officer needs to (1) certify the adequacy of internal controls and (2) designate an internal or external reviewer to conduct a periodic review of (a sample of) accounts.

- QIs that issue, trade, or are part of the payment chain of derivative instruments covered by section 871(m) (i.e., derivatives linked to US equities) need to assess their state of readiness as well as demonstrate "good faith efforts" in implementing and complying with section 871(m). Such QIs may also need to decide as to whether they should apply for the QDD status in order to avoid multiple layers of taxation on derivative payouts or underlying dividend payments.

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## Summary of the main changes

The Final QIA generally follows the proposals from Notice 2016-42 (Proposed QIA) issued in July 2016 with several notable exceptions:

| | **2014 QIA (Rev. Proc. 2014-39)** | **Proposed QIA (Notice 2016-42)** | **Final QIA (Rev. Proc. 2017-15)** |
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| Compliance certifications | Internal compliance program as part of which the responsible officer is required to make a periodic certification of internal controls. | Internal compliance program as part of which the responsible officer is required to make (1) a periodic certification of internal controls and (2) perform a periodic review of accounts by either an internal or external reviewer. | Internal compliance program as part of which the responsible officer is required to make (1) a periodic certification of internal controls and (2) perform a periodic review of accounts by either an internal or external reviewer. |
| Statistical sampling for periodic review | Statistical sampling allowed but no specific prescriptions as to the sampling methodology to be used. | Statistical sampling allowed provided that the QI has 50 or more accounts to review. The Proposed QI Agreement also included a "safe harbor" method for determining a statistical sample of accounts for the periodic review. | Statistical sampling allowed provided that the QI has 50 or more accounts to review. The Proposed QI Agreement also included a "safe harbor" method for determining a statistical sample of accounts for the periodic review. "Spot checks," whereby the internal or external reviewer reviews a subset of the sample for certain parts of the review, are allowed. |

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| Timing of certifications | Certification due by 1 July of the year following the end of the certification period. | Certification due by 1 July of the year following the end of the certification period (for example, 1 July 2018 for a certification period ending 31 December 2017). | For QIs using the third year (i.e., 2017) as the certification period for their periodic reviews, certification is due by 31 December of the year following the end of the certification period (for example, 31 December 2018 for a certification period ending 31 December 2017).<br><br>For QIs using the first or second year (i.e., 2015 or 2016) as the certification period for their periodic reviews, certification is due by 1 July of the year following the end of the certification period. |
| Term of agreement | QIA valid for three years | QIA valid for three years | QIA valid for six years |
| Validity Period for Documentary Evidence and Treaty Statements | | | Treaty statements have a three-year validity period. The Treasury Department and the IRS are considering applying the same three-year validity period to documentary evidence obtained QIs supporting an account holder's claim for treaty benefits to align with the validity period of the treaty statement. |
| Qualified Derivative Dealer regime / section 871(m) | Regime did not exist before 1 January 2017. | Section 871(m) is fully applicable from 1 January 2017. QIs have the option to become QDDs to avoid multiple layers of taxation on derivative payouts or underlying dividend payments. | Phased-in implementation of section 871(m) supplemented by the "good faith effort" rule (requiring QIs to be able to demonstrate that relevant efforts have been made in respect of section 871(m) implementation even if such implementation may not have been finalised). QIs have the option to become QDDs to avoid multiple layers of taxation on derivative payouts or underlying dividend payments. |

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| | Section 871 (m) amount: sum of the amounts by which, for each dividend on each underlying security, (A) the dividends on underlying securities associated with potential section 871(m) transactions and dividend equivalent payments that a QDD receives in its dealer capacity exceed (B) the dividend equivalent payments and the qualifying dividend equivalent offsetting payments that a QDD makes with respect to the same dividend in its dealer capacity. | Section 871(m) amount: result of the multiplication of (A) the QDD's net delta exposure to the underlying security for the applicable dividend by (B) the applicable dividend amount per share. Net delta exposure to an underlying security for an applicable dividend is the amount (measured in number of shares) by which (A) the aggregate number of shares in the underlying security that the QDD has exposure to as a result of positions in the underlying security (including as a result of owning the underlying security) with values that move in the same direction as the value of the underlying security (the long positions) exceeds the aggregate number of shares in the underlying security that the QDD has exposure to as a result of positions in the underlying security (including as a result of owning the underlying security) with values that move in the opposite direction from the value of the underlying security (the short positions). The net delta exposure calculation only includes long positions and short positions that the QDD holds in tis equity derivatives dealer business. |

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| | QDD tax liability: sum of the a QDD's section 881 tax liability for (A) its section 871(m) amount, (B) its dividends that are not on underlying securities associated with potential section 871(m) transactions and its dividend equivalent payments received as a QDD In its non-dealer capacity and (C) any payments such as interest, received as a QDD with respect to potential section 871(m) transactions r underlying securities that are not dividend or dividend equivalent payments. | QDD tax liability: the sum of (A) for each dividend on each underlying security, the amount by which its tax liability under section 881 for its section 871(m) amount exceeds the amount of tax paid by the QDD in its capacity as an equity derivatives dealer under section 881(a)(1) on that dividend, (B) its tax liability under section 881 for dividend equivalent payments received as a QDD in its non-equity derivatives dealer capacity, and (C) its tax liability under section 881 for any payments, such as dividends or interest, received as a QDD with respect to potential section 871(m) transactions that are not dividend or dividend equivalent payments to the extent the full liability was not satisfied by withholding. |
| | Timing for QDD tax liability payments: in the same time and manner as required for withholding on the applicable payments. | Timing for QDD tax liability payments: quarterly estimates of the QDD tax liability that will be added to the QI's tax liability and fling an appropriate U.S. tax return. |
| | Eligible entities: an eligible entity is: (1) a dealer in securities that is subject to regulatory supervision, (2) a bank that issues potential section 871(m) transactions to customers and receives dividends or dividend equivalent payments pursuant to potential section 871(m) transactions to hedge those transactions issued to customers; or (3) an entity that is wholly-owned by a bank and that issues potential section 871(m) transactions to customers and receives dividends or dividend equivalent payments pursuant to potential section 871(m). | Eligible entities: In additional to the eligible entities from the Proposed QIA, the following entities are also eligible to apply for the QDD status: (1) a branch, (2) a bank holding company or a wholly-owned subsidiary of a bank holding company and (3) any other person acceptable to the IRS. |

If you have any queries regarding the above, please do not hesitate to contact us.

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