Invested in America

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Re: Revenue Procedure 2017-15, Qualified Intermediary Agreement

Dear Gentlemen:

The Securities Industry and Financial Markets Association ("SIFMA")[1] appreciates the opportunity to submit comments on the Qualified Intermediary (QI) Agreement

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[1] SIFMA is the voice of the U.S. securities industry, representing the broker-dealers, banks and asset managers whose 889,000 employees provide access to the capital markets, raising over $2.4 trillion for businesses and municipalities in the U.S., serving clients with over $16 trillion in assets and managing more than $62 trillion in assets for individual and institutional clients including mutual funds and retirement plans. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

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published in Revenue Procedure 2017-15 [2] (herein, "QI Agreement" or "2017 QI Agreement"), which includes the requirements for qualified derivatives dealers ("QDDs") pursuant to regulations issued under section 871(m) of the Internal Revenue Code (the "Code").

SIFMA submitted a comment letter dated August 31, 2016, in an effort to provide constructive recommendations on the proposed QI Agreement that would be operationally administrable. SIFMA appreciates that many of those recommendations were included in the 2017 QI Agreement. In that same spirit, we provide the following comments on the 2017 QI Agreement.

I. Requirements of QDDs

A. Net delta exposure- reliance on calculation used for non-tax business purposes

Our members request clarity on the extent to which a QDD may rely on the net delta calculation it uses for non-tax business purposes. Specifically, we request clarification that the net delta calculation that is used today for non-tax business purposes may be used for tax purposes subject *only* to the modifications specifically enumerated in section 2.47 of the 2017 QI Agreement and Treas. Reg. § 1.871-15(q)(4). This clarification is necessary because the net delta calculation utilized by many members today for non-tax business purposes will, among other things, (1) determine overall exposure to an equity security or index, and (2) exclude securities lending and sale-repurchase transactions.

Given that the net delta calculation permits the use of the calculation used today for non-tax business purposes, we request confirmation that QDDs have flexibility to determine its net delta exposure on a constituent level or at the index level so long as it is consistent with their net delta calculation for non-tax business purposes. If for example, a QDD enters into a delta-one short position with respect to an exchange traded fund or qualified index and then hedges its short position by holding delta-one long positions in the components of the fund or index, it is unclear whether the QDD can determine its net delta in respect of the components of the fund or index because the section 871(m) regulations do not look through to the components of the exchange traded fund or qualified index. The net delta calculation performed today by many equity derivatives dealers would generally look through a fund or index in order to net these positions down and give a more accurate risk assessment. Given that the net delta calculation permits the use of the calculation used today for non-tax business purposes, we request clarification that dealers looking through to the components of funds or indices in order to isolate exposure to a given equity security is consistent with the definition of net delta exposure provided in the QI Agreement and may be relied upon.

On the other hand, dealers will generally hedge index trades where there is an exchange traded fund that hedges the same index with shares of the exchange traded fund and for non-tax business purposes a dealer may compute the net delta at the index level or at the underlying component security level, depending on the dealer. Dealers should have the

[2] Rev. Proc. 2017-15, 2017-3 I R.B. 437.

flexibility to calculate net delta at the index level consistent with their practices for non-tax business purposes.

Further, SIFMA requests that the QDD rules be clarified to provide that securities lending and sale-repurchase transactions should not be included in the net delta exposure calculation for tax purposes if these transactions are not included in the net delta calculation for non-tax business purposes. The net delta calculated today for non-tax business purposes does not include (and is not required to include for regulatory purposes) these transactions because net delta will always be zero. Since the QDD will not have a QDD tax liability related to these transactions there is no benefit to introducing the additional complexity of making adjustments to the net delta calculation relied on today for non-tax business purposes in order to include securities lending and sale-repurchase transactions in the calculation. Since neither the QI Agreement nor the regulations require such adjustment to be made, we request that the QDD rules be amended to clarify that a QDD whether solely engaging in securities lending and sale-repurchase transactions or also engaging in other U.S. equity-linked transactions may exclude securities lending and sale-repurchase transactions from the net delta exposure tax calculation to the extent that these transactions are excluded from the net delta calculation for non-tax business purposes.

B. Net delta exposure – interbranch transactions

Our members appreciate Treasury and the IRS's inclusion of the net delta exposure for purposes of determining the section 871(m) amount of the QDD tax liability. We seek clarification regarding the computation of QDD tax liability based on the definition of net delta exposure under section 2.47 of the 2017 QI Agreement and Treas. Reg. § 1.871-15(q)(4), specifically the requirement to only take into account transactions that "exist and are attributable to that QDD for U.S. federal income tax purposes."[3]

The 2017 QI Agreement provides that an entity must enter into (or continue) a QI Agreement and any home office or branch of the entity that desires QDD status must separately meet the requirements of an eligible entity as if it were a separate entity. Accordingly, each branch of an entity is treated as a separate QDD.[4] For purposes of the QDD tax liability, the QDD's net delta exposure to an underlying security is the number of shares by which a QDD's aggregate long position exposure to an underlying security in its dealer capacity exceeds its aggregate short position exposure to the underlying security in its dealer capacity. Each QDD must determine its net delta exposure separately, only taking into account transactions that "exist and are attributable to that QDD for U.S. federal income tax purposes." The required adjustment suggests that transactions between branches (including disregarded entities with the same owner) would be disregarded as interbranch transactions are generally not relevant for U.S. income tax purposes.[5] Consequently, in a back-to back transaction between branches, the net delta

[3] Section 2.47 of the 2017 QI Agreement and Treas. Reg. § 1.871-15(q)(4).

[4] See section 2.63 of the 2017 QI Agreement providing that "each home office or branch that obtains QDD status is treated as a separate QDD."

[5] Our members note that another interpretation, which is consistent with our request, is that the principle of separate entity treatment applies to the net delta exposure of each QDD and thus a

exposure will always be positive or overstated for one branch and negative or understated for the other branch, which correspondingly results in a positive QDD tax liability for one branch and a zero QDD tax liability for the other branch, even when the net delta exposure for each of the branches considered separately with respect to the transaction, and for the entity of which the branches are a part, might otherwise be delta flat or zero.

SIFMA requested the use of net delta because it is a more accurate reflection of the QDD's positions with respect to an underlying security than the calculation that was provided in the draft QI Agreement.[6] However, the adjustment to net delta exposure requiring the exclusion of interbranch transactions diminishes the accuracy of the net delta exposure and may unnecessarily result in an additional level of tax included in the QDD tax liability for interbranch transactions. Given that the net delta calculation is a measurement of residual exposure to an underlying security, there should be parity between the tax treatment of a QDD branch's transaction with a regarded entity or with an entity disregarded for U.S. tax purposes, if the economic results of each transaction are the same.

Any policy reason for disregarding interbranch transactions when performing the QDD tax liability calculation is unclear, especially when there is precedent in the tax regulations for respecting interbranch trades. For example, Prop. Treas. Reg. §1.863-3(h) (the proposed Global Dealing regulations) allows each branch to be treated as a separate person and income to be allocated among multiple branches and sourced accordingly by treating the branches as separate persons. Further, the QI Agreement and Treas. Reg. §1.1441-1T(e)(6)(i)(F) provides that "each home office or branch that obtains QDD status is treated as a separate QDD."[7] Given that the QDD rules require each branch to be treated as a separate entity and separately compute a QDD tax liability, interbranch transactions between two QDDs also should be treated as transactions between two separate persons when calculating the QDD tax liability. Accordingly, we request that the principle of separate person treatment also apply to the net delta exposure calculation, and transactions between branches be respected in that context.

C. Dividend withholding

1. Request for exemption from withholding on dividends

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transaction between QDDs that are branches would be respected on a hypothetical basis for U.S. federal income tax purposes but only for purposes of determining each QDD's net delta exposure.

[6] I.R.S. Notice 2016-42, 2016-29 I.R.B. 67. See section 2.80 of Proposed QI Agreement providing "The "section 871(m) amount" is computed by determining, for each dividend on each underlying security, the excess (if any) of (A) the amounts the QDD receives in its dealer capacity that are dividend equivalent payments and dividends on underlying securities associated with potential section 871(m) transactions over (B) the dividend equivalent payments and the "qualifying dividend equivalent offsetting payments"[6] that the QDD makes or is contractually obligated to make in its dealer capacity with respect to the same underlying dividend."

[7] See section 2. 63 of the QI Agreement and Treas. Reg. §1.1441-1T(e)(6)(i)(F)

We request that the exemption from withholding on payments of U.S. source dividends to QDDs provided in prior versions of the regulations[8] be reintroduced in order to eliminate overwithholding in a chain of dividends and dividend equivalents. If this proposal is adopted, the QDD would be liable solely for its 871(m) amount on its net delta exposure with respect to its dealer activity.

The current framework seems to favor hedging through a derivative transaction over holding the physical stock since a QDD is exempt from withholding on dividend equivalent payments but not actual dividends. Both the statute and the previous versions of the regulations recognize that dealers generally enter into section 871(m) transactions and hold underlying securities to mitigate exposure to client trades and thus they provided an exception to withholding for any dividends and dividend equivalents received in an equity derivatives dealer capacity. While we appreciate that in some instances, withholding might not be required on the client transaction, we do not interpret the statute to limit a withholding exemption for a qualified dealer on such basis as section 871(m)(6) provides the Secretary complete authority to "reduce such tax … as the Secretary determines is appropriate to address the role of financial intermediaries in such chain."[9] Further, section 871(m)(6) treats dividends the same as dividend equivalents, and Treasury and the IRS have exempted QDD's from withholding on dividend equivalent amounts under the authority of this paragraph.

Because of the complexities of the section 871(m) regulations in addressing grandfathered trades, indices and exchange traded funds, the withholding rules which provide relief for certain clients based on their tax status, and dealer hedging on a dynamic and macro basis, it is difficult to determine whether dividends received on a hedge are traceable to a client trade that resulted in withholding tax. Accordingly, any methodology that attempts to determine whether withholding tax was suffered by at least one party in a chain of transactions will be inaccurate and result in instances of overwithholding. Also, any policy reason for limiting the withholding exemption to dividend equivalent payments should be outweighed by the practical consideration that tax should not have a disproportionate influence on hedging strategies. The fact that a QDD is a financial intermediary that may receive income from dividends but either has an offsetting payment to a customer or would pay a QDD tax liability on the section 871(m) amounts, should be sufficient to allow an exemption from withholding on dividends based on the authority provided in the statute.

2. Alternative requests to offset QDD tax liability under section 881(a)(1)

Although we request a withholding exemption on dividends paid to QDDs for the reasons described above, in an effort to provide other workable solutions, we alternatively request that a QDD determine its section 881(a)(1) tax liability on dividends and deemed dividends received in its capacity as an equity derivatives dealer by reducing its potential tax liability for dividends and deemed dividends received by its withholding tax liability for dividend equivalents paid to account holders. We also request a coordination rule between the section 881(a) tax liability and section 871(m) amount tax liability by

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[8] T.D. 9734, 2015-41 I.R.B. 500.

[9] I.R.C. Section 871(m)(6).

providing that the QDD tax liability is the greater of its section 871(m) amount tax liability or the section 881(a) tax liability (as determined by the calculation described in the preceding sentence).

The preamble to the QI Agreement provides that a QDD will be subject to withholding on dividends (including deemed dividends) received on or after January 1, 2018 and that Treasury and the IRS will consider comments recommending approaches for alleviating any overwithholding (and preventing any underwithholding) that might occur when withholding on dividends begins in 2018. Further the preamble to the final and temporary regulations provides that Treasury and the IRS are concerned that an exemption for QDD from withholding tax on dividend income "when combined with the net delta exposure method, could result in U.S. source dividends escaping U.S. tax completely in certain circumstances."

The allowance described above permits the QDD to offset its potential liability to the extent there is a dividend equivalent payment subject to withholding made to an account holder, the amount of which is substantiated by the Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding, filed by the QDD. Because of recent non-tax pressures to eliminate intercompany (and interbranch) hedging transactions as well as the inclusion of securities lending transactions in the QDD regime, it is critical that financial institutions have sufficient alternatives to prevent excessive withholding in a chain of transactions.

Accordingly, we request an allowance for a QDD to determine its tax liability under section 881(a)(1) on dividends and deemed dividends received in its capacity as an equity derivatives dealer by offsetting the amount of potential tax on dividends and deemed dividend received by the amount of actual tax applied to dividend equivalents paid to account holders with respect to section 871(m) transactions. Our members also request a coordination rule between the section 881(a) tax liability and section 871(m) amount tax liability by providing that the QDD tax liability is the greater of its section 871(m) amount tax liability or the potential section 881(a) tax liability.

Given the difficulty of performing this calculation on a dividend by dividend or underlying security by underlying security basis, we also request that this determination be based on the potential amount of withholding on total dividend received less total amount of withholding actually applied to dividend equivalents payments made for the calendar year. Further, given the difficulty in determining whether to characterize a payment as a dividend or substitute dividend, we request that a QDD be permitted to treat all the payments made on securities lending and sale-repurchase transaction as dividend equivalents for purposes of the calculation. Lastly, we also request that a QDD be exempted from withholding on dividends and self-assess its section 881(a) tax liability in accordance with the offset allowance described in the preceding sentences to ensure that to the extent a QDD receives actual dividends, a single level of tax is applied on either the actual dividends received on the dealer hedges or the dividend equivalents paid on section 871(m) transactions.

For example, a QDD has a client trade with another QDD over a basket of U.S. equities with a notional of $100. The QDD hedges that exposure by acquiring $50 of the

respective components of the baskets and $50 derivatively. As the QDD has a 0 net delta exposure (delta flat), its section 871(m) amount is zero but it would self-assess its 881(a)(1) tax liability on dividends with respect to its $50 of physical stock positons. If the client trade is instead subject to withholding under 871(m), then the QDD tax liability would be zero as it would not have a tax liability for its section 871(m) amount or under section 881(a)(1) (assuming the client and the QDD have the same withholding tax rate, there would be withholding on the client trade with the notional of $100). If the QDD client trade instead only had a notional of $50, then the QDD tax liability would be its tax liability for its section 871(m) amount of $50 as it would not have a section 881(a) tax liability (assuming the client and the QDD have the same withholding tax rate, there would be withholding on the client trade with the notional of $50).

If the QDD client trade instead only had a notional of $25, assuming still that the QDD hedges that exposure by acquiring $50 of the respective components of the baskets and $50 derivatively, then the QDD tax liability would be its tax liability for its section 871(m) amount of $75 as that amount would exceed the amount of its section 881(a) tax liability (assuming the client and the QDD have the same withholding tax rate, the withholding on the client trade with the notional of $25 which would only offset half of the potential withholding on the actual dividends received on $50 of shares). If there was an additional QDD client trade with another QDD with a notional of $75, then the QDD would self-assess its tax liability for its section 881(a) tax liability with respect to dividends received on $25 of shares (assuming the client and the QDD have the same withholding tax rate, the withholding on the client trade with the notional of $25 would only offset half of the potential withholding on the actual dividends received on $50 of shares) as that amount would exceed the amount of its section 871(m) amount of zero.

D. QDD status for potential section 871(m) transactions and draft Form W-8IMY, Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain U.S. Branches for United States Tax Withholding

The QI Agreement provides that a QDD must act as such for all potential section 871(m) transactions and underlying securities[10]. This would seem to require a QDD to provide a Form W-8IMY representing QDD status for all payments made with respect to potential 871(m) transactions and dividend income from underlying securities.[11] Treas. Reg.

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[10] See section 1.01 of the QI Agreement providing "If QI acts as a QDD with respect to the home office or branch, the home office or branch, as applicable, must act as a QDD for all payments made as a principal with respect to potential section 871(m) transactions and all payments received as a principal with respect to potential section 871(m) transactions and underlying securities, excluding any payments made or received by the QDD to the extent the payment is treated as effectively connected with the conduct of a trade or business within the United States within the meaning of section 864."

[11] See section 6 of the QI Agreement providing "If QI is acting as a QDD for payments with respect to potential section 871(m) transactions or underlying securities, it must certify that it is acting as a QDD for those payments and assumes primary chapters 3 and 4 withholding responsibility and primary Form 1099 reporting and backup withholding responsibility for any payments with respect to potential section 871(m) transactions that it makes as required by this

§1.1441-1T(b)(4)(xxii) provides that a withholding agent is not required to withhold on a properly documented QDD for "(A) A payment with respect to a potential section 871(m) transaction that is not an underlying security; (B) A payment of a dividend equivalent; or (C) A payment of a dividend in 2017."

Many QDDs would prefer to be withheld upon as was done in prior tax years for U.S. source fixed, determinable, annual, or periodical (FDAP) income that is not a dividend or dividend equivalent payment. U.S. withholding agents already have the infrastructure in place to withhold on these payments. Further, QDDs do not want to develop systems to track and self-assess tax. Accordingly, we request that the regulations be revised to require a withholding agent to withholding on U.S. source FDAP payments other than dividend and dividend equivalent payments made to a QDD.

Further, the instructions to the draft Form W-8IMY provide the following: "A QDD that receives payments for which the QDD is entitled to a reduced rate of withholding under an income tax treaty may use its Form W-8IMY to both certify its status as a QI acting as a QDD and to claim treaty benefits with respect to such payments… To make a claim for treaty benefits in such a case, the QDD should provide a withholding agent with a statement associated with its Form W-8IMY that contains the information required in Part III of Form W-8BEN-E." We agree that providing two withholding certificates for the same transaction is operationally difficult to implement and appreciate being able to provide a statement along with the Form W-8IMY. However, it is burdensome on withholding agents to develop a process to validate bespoke statements which can vary in information provided. Given the details required in Part III of the Form W-8BEN-E, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities), as well as the special provisions, we request that the Form W-8IMY be updated to include details in Part III of the Form W-8BEN-E. We also request that the treaty statement be valid indefinitely under the same conditions of the Form W-8IMY until there is a change in circumstances.[12]

E. Reconciliation Schedule

Our members request clarification on the requirement to maintain the reconciliation schedule in "any manner or format that permits the IRS to reconcile the amount reported by the QDD for the calendar year." It is unclear how the reconciliation schedule differs from the general record-keeping requirements of Treas. Reg. §1.6001-1. Given that the net delta exposure, absent some adjustments, is the net delta calculation used for non-tax business purposes, many QDDs were going to leverage their current systems to perform the calculation and additional procedures to make the required adjustments. The detailed information seemingly required by the reconciliation schedule seems to necessitate additional substantiation. Further, the amount of information currently required under the reconciliation schedule is extensive (e.g., the QDD's long positions and short positions). It is unclear why this is required, especially since the section 871(m) amount is now based on the net delta calculation. We request that the QDD instead maintain documentation to

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Agreement, and it must provide all other information required by Form W-8IMY with respect to the certification."

[12] Treas. Reg. §1.1441–1T(e)(4)(ii)(B).

support the net delta calculation process and that only the general record-keeping requirements of Treas. Reg. §1.6001-1 apply to the QDD tax liability computation.

F. Reporting of QDD tax liability

Our members request that the QDD tax liability be reported on Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons. While we appreciate that the Form 1042 is for withholding tax liability, for operational reasons we prefer the use of the Form 1042. First, the persons familiar with QDD and the requirements of the QDD tax liability are largely the same persons responsible for Form 1042 reporting. The persons responsible for U.S. income tax return filings such as the Form 1120-F, U.S. Income Tax Return of a Foreign Corporation, would need to be educated and trained and controls would need to be put in place to ensure the inclusion of the QDD tax liability and estimated payments. We also think that this approach is sensible because the dividend equivalents and, in 2017, the actual dividends received by a QDD, will be reported to the QDD using the QI/QDD EIN, not the corporate EIN. Further, if the QDD is a partnership, additional guidance would be needed to understand how the QDD tax liability should be reported. For these reasons, we request that the QDD tax liability be reported on Form 1042.

G. Form 1042-S Reporting to another QDD

We request that withholding agents that are not QDDs and QDDs have parallel information reporting requirements for payments made to QDDs. Treas. Reg. §1.1461-1(c)(2)(ii)(J) provides, "except as provided in §1.1461–1(c)(2)(i)(M), any payment to a qualified derivatives dealer when the withholding agent is not required to withhold on the payment pursuant to §1.1441–1(b)(4)(xxi), (xxii), or (xxiii). This exception does not apply to withholding agents that are qualified derivatives dealers." Treas. Reg. §1.1461-1(c)(2)(i)(M) requires reporting of "any dividend or any payment that references a dividend from an underlying security pursuant to a securities lending or sale-repurchase transaction paid to a qualified derivatives dealer even when the withholding agent is not required to withhold on the payment pursuant to §1.1441–1(b)(4)(xxi), (xxii), or (xxiii)." Under the QI Agreement, section 8.02(I) requires a QI acting as a QDD to report on a specific recipient basis amounts paid to another QDD.

Essentially, whether to treat a QDD as a recipient of Form 1042-S reporting is dependent on whether the withholding agent is a QDD. Many financial institutions rely on the same information reporting systems and personal to perform Form 1042-S reporting for the multiple withholding agents in their institution. It is operationally burdensome to revise system logic or create manual processes to perform the additional reporting required if the withholding agent is a QDD. Given that Treasury and the IRS have eliminated the reporting requirement for withholding agents other than QDDs, there does not appear to be any compliance benefit to the additional reporting required by QDDs. Further, we support the approach taken by the regulations as many non-QDD withholding agents will not otherwise be able to comply with the requirement to report to QDDs. Therefore, in order to achieve a consistent reporting framework, we request that the QI Agreement and regulations be amended to remove the requirement for QDDs to report dividend equivalent payments made to other QDDs.

II. Requirements of QIs

A. QIs that entered into QI Agreement to obtain QDD status for disregarded entity or branch

We understand that a disregarded entity or branch of a non-U.S. financial institution cannot separately apply for QI status, and, therefore, in order to obtain QDD status an application must be submitted by the entity rather than its branch. Similarly, in the case of a disregarded entity, the application must be submitted by the single member owner. We request clarification that when the other branches (including the home office) of the entity do not maintain QI designated accounts and do not act as QDDs, these other branches do not have any compliance obligations under the QI Agreement. We request the same clarification for a regarded owner that applies for QI status only so that its disregarded entity may function as a QDD branch.

The compliance obligations of a QI, specifically the certification of internal controls and periodic review requirement, require a review of nonqualified intermediary compliance and FATCA compliance, which adds substantial administrative burdens and compliance costs. While we accept that a review of general compliance obligations may be required for the branch or disregarded entity that obtains QDD status, we request clarification that the other branches or regarded owner, or other disregarded entities (and their branches) with the same regarded owner, with no QI or QDD activity have no such requirement.

B. Expiration of limitation on benefits statements and potential expiration of documentary evidence

The QI Agreement introduces a three-year validity period for treaty statements associated with documentary evidence for establishing residence in a treaty country.[13] Neither the 2016 proposed QI Agreement nor prior QI Agreements required resoliciting treaty statements absent a change in circumstances. Further, the preamble to the 2017 QI Agreement states that Treasury and the IRS are considering applying a three-year validity period to documentary evidence obtained by QIs to establish an account holder's claim for treaty benefits. A three year re-solicitation requirement for treaty statements and, potentially, documentary evidence is unnecessary and burdensome given the unlikeliness of a change in the account holder's information. For instance, an entity that meets the publicly traded corporation, subsidiary of publicly traded corporation, or government entity limitation on benefits provisions of the applicable treaty is unlikely to need to update treaty information every three years. This is also the case with documentary evidence, like Articles of Incorporation or other formation documents. Accordingly, there is little value to the IRS in departing from AML/KYC practices and the general allowance provided in prior agreement that treaty statements and documentary evidence generally do not expire. The requirement of account holders to notify the QI of a change in circumstances is sufficient to address any changes to account holder information or treaty claims. We request that the three-year validity period for treaty statements be removed

[13] Section 5.11(A) of the 2017 QI Agreement.

from the QI Agreement and that no changes are made to current rules regarding the validity period of documentary evidence

C. Due diligence standard change to review all "account information"

Prior QI agreements, and the 2016 proposed QI Agreement, set forth the general standards of knowledge requirements of a QI to validate a claim of foreign status and, if applicable, treaty benefits. (i.e., U.S. mailing or residence address) and these requirements applied to the QI's "account holder." However, the 2017 QI Agreement, as a result of cross-referencing the standards of knowledge of Treas. Reg. §1.1441-7T(b)(3), now requires a QI to apply the standards of knowledge to any "account information." As a result, many claims of accounts holders will be invalidated. The prior QI agreements recognized that it is too burdensome to cure account file conflicts that relate to persons other than the QI's direct account holders. Further, QIs do not have the resources to apply the standards of knowledge to the account files of an account holder.

It is our understanding that this change was not intentional, but rather a result of replacing certain text of the QI Agreement with cross-references to the regulation (which often contains an embedded cross-reference to another regulation). Because of the complex drafting style of the U.S. tax regulations, it is very challenging for QIs to understand the implications of cross-references to the regulations. For this reason, prior QI Agreements contained a comprehensive rule set for QIs to follow with limited cross-references to the regulations.

Accordingly, our members request the QI Agreement revert to the prior standard of requiring QIs to apply the standards of knowledge at the account holder level. We also request that the QI Agreement be amended to provide a comprehensive set of rules for the QI rather than cross-references to regulations.

D. Potential 871(m) notification for intermediaries (including QIs) not acting as QDDs

The QI Agreement requires a QI acting as a QDD to notify payees that it will withhold on dividend equivalent amounts at the time of the dividend payment date.[14] Treas. Reg. §1.1441-2T(e)(7)(v) includes a similar requirement for all "intermediaries" and flow-through entities that receive a dividend equivalent payment from an upstream withholding agent that has made an election under Treas. Reg. §1.1441-2T(e)(7)(iv) to withhold on the dividend payment date. It is unclear, however, if this requirement applies to QIs. Other sections of the regulations refer to QIs specifically rather than a general inclusion through reference to intermediaries. Further, the notification requirements for intermediaries are not included (either directly or by cross-reference) in the QI Agreement.

We request clarification that the notification requirement of Treas. Reg. §1.1441-2T(e)(7)(v) does not apply to QIs that are not acting in the capacity of QDDs. QIs receive payments from numerous withholding agents on behalf of various account holders and it would be impossible to track and maintain this notification requirement.

[14] Section 3.03(B) of the 2017 QI Agreement.

E. Mandatory reporting of separate Forms 1042-S to account holders, upon request, in cases of overwithholding

The QI Agreement provides that if there has been overwithholding, and the QI does not apply for a collective refund, the QI must, upon request, provide an account holder with a payee-specific Form 1042-S.[15] While we appreciate that this requirement enables an account holder to claim a refund of the excess withholding either directly or through the QI, there are no clear time limits to the reporting imposed upon the QI. A QI will need to file amended returns in order to facilitate a refund claim. Without any time limitation, a QI does not have the ability to limit or control requests from account holders that will naturally be made at different times and possibly require the filing of several amended returns. Further, the QI Agreement does not allow the QI to refuse the account holder's request even when a refund is not available because, for instance, the statute of limitation has expired or the account holder has no intention of obtaining a TIN.

Accordingly, we request that a QI be required to provide a separate Form 1042-S only if the request is received by the QI by August 15 of the year after the year of the overwithholding, and only if the QI chooses not to include the customer in a collective refund claim. The August 15 deadline, which is one month before the extended due date for filing the Form 1042, provides the account holder with a reasonable amount of time to make their request to the QI and eliminates the operational burden associated with multiple or amended Form 1042 filings. Furthermore, as a condition for producing a separate Form 1042-S, a QI should be allowed to require a beneficial owner to furnish a Form W-8BEN / BEN-E, which must include a U.S. TIN. By including a U.S. TIN on the Form W-8BEN / BEN-E, the separate Form 1042-S can also include that TIN. Without the TIN on the Form 1042-S, the IRS will generally refuse any refund claim.

III. Conclusion

Our members appreciate your consideration of their views and concerns, and they would appreciate the opportunity to discuss the issues in this submission with you and your colleagues. Please do not hesitate to contact me at (202) 962-7333 or ppeabody@sifma.org, or SIFMA members' outside consultant Tara Ferris at Ernst & Young, who can be reached at (212) 360-9697 or tara.ferris@ey.com.

Sincerely,

Payson Peabody
Managing Director & Tax Counsel

[15] Section 9.04 of the 2017 QI Agreement.