

Qualified Intermediaries

US reporting and compliance alert

Intensive focus on the Qualified Intermediary program

dated August 2008

The QI program has recently been the focus of several discussions involving the IRS, the US legislator and some international accounting firms. The much broadcasted purpose was to set up potential enhancements to the QI regime in order to prevent tax avoidance techniques used by certain US taxpayers. As a result, revised QI rules are expected before the year end.

Background

The first effective step was the study realized by the US Government Accounting Office ("GAO") in late 2007. The GAO had indeed been asked to assess whether weaknesses existed in the US withholding system for US source income and to identify any weaknesses in QI external reviews and IRS's use of program data. They concluded that although the QI program provided some assurance that taxes on foreign investors were withheld and reported, the program needed to be improved.

On July 8th, the IRS held a conference call with six large accounting firms to discuss the role of the accounting community in conducting QI audits and detecting and reporting QI's actions. The US Senate Homeland Security and Government Affairs Permanent Subcommittee on Investigations (PSI) and the Senate Finance Committee then held several hearings based on which reports were prepared by the staff of the Joint Committee on Taxation (E.G. JCT Report 7/2008 – Selected Issues Relating to Tax Compliance With Respect to Offshore Accounts and Entities; PSI report 7/2008 – Tax Haven Banks and US Tax Compliance). Those reports again emphasized some needed enhancements to the QI regime.

Purpose

This procedure is expected to result in a tightening of the reporting obligations and oversight of internationally headquartered financial institutions. The IRS wants to ensure that foreign banks do appropriately confirm the identities of US investors, notify the IRS of income earned in the accounts and, in some cases, withhold and remit taxes on that income. The responsibilities of external auditors will also be expanded in the scope of the QI audits.

What should QIs expect?

The possible changes that are being considered are the following:

- Require QIs to determine and report (1099 reporting) all accounts beneficially owned by US persons, even if the accounts are held in the name of a foreign corporation, trust, foundation or other shell entity;
- Require QIs to report foreign-source income, as well as US source-income received by US customers who are not otherwise exempt from information reporting and backup withholding;
- Require QIs to apply to their QI reporting obligations all information obtained through their KYC procedures;
- Require more electronic filing of forms under QI program;
- Expand the scope of QI audits and require external auditors to identify and report evidence of fraud or illegal acts.

We anticipate that the draft revised QI rules will be issued between end of August and October 2008. QIs may wish to examine their US client-related activities and procedures beforehand, in order to determine any relevant modifications to be realised in light of these new developments.

The changes in the QI audit guidelines are likely to take effect next year (i.e. for financial year 2008).

In addition to this process, the IRS is still focused on securities lending withholding and reporting and the draft rules for these are also likely to be issued shortly.

Contacts

For further information, please contact the PricewaterhouseCoopers Luxembourg Qualified Intermediaries expert:

Kerstin Thinnes

Tax Partner,
+352 49 48 48-2537

kerstin.thinnes@lu.pwc.com

Marianne Weydert

Audit Partner,
+352 49 48 48-2566

marianne.weydert@lu.pwc.com

PricewaterhouseCoopers

400, route d'Esch, B.P. 1443
L-1014 Luxembourg
Telephone +352 49 48 48-1
Facsimile +352 49 48 48-2900

PricewaterhouseCoopers cannot be held liable for mistakes, omissions, or for possible results obtained further to the use of this document, which is issued for information purposes only. No reader should act on or refrain from acting on the basis of any matter contained in this publication without considering and, if necessary, taking appropriate advice upon their own particular circumstances.

© 2008 PricewaterhouseCoopers S.à r.l. All rights reserved. PricewaterhouseCoopers refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.