

## Foreign Account Tax Compliance Act: QI-Status and FATCA-Status

### Introduction

In the last newsletter of August 2010 you received an overview of FATCA. The following newsletter will deal with the links between the existing QI-status and the future FATCA-status of financial institutions.

### QI-Status

For financial institutions, which have entered into a Qualified Intermediary (QI) agreement with the US-tax authorities (IRS), there are basically two different statuses:

- „QI with primary withholding responsibility“: the QI takes the responsibility to withhold taxes and to do the related reporting.
- „QI without primary withholding responsibility“: Taxes are withheld by the withholding agent or the custodian, the QI has certain reporting duties.

Financial institutions that do not have a QI-agreement with the IRS still have reporting obligations towards the withholding agent. The QI-regulations will remain valid even after the implementation of FATCA; the FATCA-rules are designed to close loop-holes in the QI-rules.

### FATCA-Status

The IRS-bulletin 2010-37, which has been published on September 13<sup>th</sup> 2010, gives an overview on the different FATCA-statuses. In the following, we limit ourselves to the „Foreign Financial Institutions“ (FFI). To be a FFI according to FATCA one has to meet at least one of the following criteria:

- To accept deposits in the ordinary course of a banking or similar business
- To hold financial assets for the account of others as a substantial portion of its business (e.g.: asset manager)
- To be engaged primarily in the business of investing, reinvesting, or trading in securities, partnership interests, commodities or any interest (including a futures or forward contract or option) in such securities, partnership interests, or commodities (e.g.: broker)

FFIs are divided into two groups:

- „Participating FFI“: a FFI that enters into an agreement with the IRS, in which the obligations in regard to client identification, reporting and auditing are regulated.
- „Non-participating FFI“: a FFI that has not entered into an agreement with the IRS.

A participating FFI may opt for the „Election to be Withheld upon“, such a FFI does not withhold taxes on payments out of US-sources, but has the withholding agent or the custodian to withhold taxes and to do the payments to the IRS (comparable with the status of a „QI without primary withholding responsibility“). The exact rules for this option are not yet clear.

### Courses of action

The courses of action have to be checked whether they correspond with the FATCA-strategy chosen by the FFI. Also they have to be evaluated in respect to their feasibility. Certain courses of action can be taken without any further constraints besides the related costs (e.g.: necessary adjustments in IT-systems). Some of the courses of action however will result in considerable additional requirements and problems when implementing and operating them. A FFI who currently has the status of a „QI with primary withholding responsibility“ and opts to become a FFI with „election to be withheld upon“ for example, should be aware that the implementation and the operating of differing tax withholding concepts can result in considerable additional costs and risks (e.g.: tax withholding by the broker in stock exchange transactions). The same is also valid for a „QI without primary withholding responsibility“ who decides to become a „FFI without election“. A FFI with a QI-agreement who does not want to enter into a FATCA-agreement must face termination of the QI-agreement.

In the following table the different courses of action regarding the future FATCA-status, depending on the current QI-status are presented:

		Future FATCA-Status		
		Participating FFI without election	Participating FFI with election	Non-participating FFI
Current QI-status	QI with primary withholding responsibility	✓	(✓)	(✓)
	QI without primary withholding responsibility	(✓)	✓	(✓)
	Non-QI	(✓)	(✓)	✓

Assessment of implementability:

- ✓ Implementation possible without constraints
- (✓) Implementation difficult or possible only with constraints (eg: relinquishment of QI-status)

### Participate or not?

For the decision of a FFI to enter into a FATCA-agreement with the IRS, different questions have to be considered:

- Does the FFI want to be active in the business with US-clients and US-securities?
- Are the costs for implementing the FATCA-rules and complying with them justified by real or potential income out of the business with US-clients and US-securities?
- Is the FFI owned by an US-company or does the FFI have substantial ownership by US-persons?
- Does the FFI belong to a group of companies which is active in the US-business itself or over other companies belonging to that group?
- Does the FFI maintain business-relationships with US-companies whose termination could have a negative impact on the reputation?
- Which QI-status does the FFI have?

The next FATCA-newsletter, which will be published in the middle of November 2010, will focus on the requirements of FATCA in regard to client identification and documentation.

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