

# New Year's Gifts: IRS Issues Final 2023 QI Agreement and Additional Code Sec. 1446(f) Guidance

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In December 2022, the U.S. Internal Revenue Service (“IRS”) issued Rev. Proc. 2022-43, which provides the final qualified intermediary (“QI”) agreement.<sup>1</sup> The prior QI agreement<sup>2</sup> (the “2017 QI Agreement”) expired at the end of 2022. The new QI agreement (the “2023 QI Agreement”) came into effect on January 1, 2023, and is set to expire on December 31, 2028.

The 2023 QI Agreement includes significant updates compared to the 2017 QI Agreement. First, and most notably, the 2023 QI Agreement largely adopts the changes proposed by the IRS in 2022 in Notice 2022-23 (commonly referred to as the “QI Rider”), which included proposed modifications relating to a QI’s ability to act in such capacity with respect to receiving certain amounts from interests in publicly traded partnerships (“PTPs”)<sup>3</sup> and the QI’s withholding obligations under Code Secs. 1446(a) and 1446(f) of the Internal Revenue Code (the “Code”). In addition, the 2023 QI Agreement incorporates prior IRS guidance, a significant portion of which was published in the form of Frequently Asked Questions (“FAQs”). For example, the 2023 QI Agreement includes additional guidance relating to the requirements for QIs acting as qualified derivatives dealers (“QDDs”) or as intermediaries with respect to dividend equivalent payments under Code Sec. 871(m), as well as modifications to a QI’s periodic certification requirements. Lastly, the 2023 QI Agreement incorporates new obligations of a QI. Many of these changes are addressed herein.

The IRS also released Notice 2023-8 (the “Notice”) in December 2022, which provides additional guidance for brokers to comply with certain Code Sec. 1446 requirements that relate to withholding on the transfer of an interest in a PTP. The Notice provides that a QI applying the provisions of the 2023 QI Agreement may also rely on specified provisions of the Notice.<sup>4</sup> This article also discusses the Notice.



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## The 2023 QI Agreement

### “Best Efforts” Standard for Collecting U.S. Taxpayer Identification Numbers for Purposes of Code Secs. 1446(a) and (f)

The 2023 QI Agreement adopts a “best efforts” approach to the collection of U.S. taxpayer identification numbers (“TINs”) from non-U.S. persons holding interests in PTPs. (This update was adopted largely in response to comments received by the IRS relating to the practical challenges that QIs may face with respect to the collection of U.S. TINs.) The 2023 QI Agreement provides solicitation requirements that QIs must apply for collecting U.S. TINs from account holders holding PTP interests. Specifically, a QI is treated as having applied its “best efforts” to obtain a U.S. TIN when the QI makes a written solicitation (initial solicitation) for the account holder’s U.S. TIN in 2023 or the calendar year in which an account holder acquires a PTP, and if an account holder’s U.S. TIN is not provided based on the initial solicitation, the QI is required to make an additional written solicitation for the account holder’s U.S. TIN in the calendar year following the calendar year of the initial solicitation, and, if necessary, a further written solicitation in the calendar year following the year of the additional solicitation.<sup>5</sup> The 2023 QI Agreement’s definition of “material failure” and “event of default” were similarly updated to take into account this “best efforts” standard with respect to the collection of U.S. TINs for purposes of Code Sec. 1446. QIs (and certain entities acting in an NQI capacity) should consider whether it is appropriate to update their policies and procedures to take into account these new U.S. TIN solicitation requirements.

The “best efforts” standard relates to documentation and not withholding. It is important to note that a QI is not permitted to apply a reduced rate of withholding under Code Sec. 1446(a) or (f) if the account holder fails to provide a U.S. TIN for any calendar year in which a payment is made.

### Requirements for Disclosing QIs

The 2023 QI Agreement incorporates the concept of a “disclosing QI,” which is a QI that does not assume primary withholding responsibilities for purposes of Code Secs. 1446(a) and (f), and, instead, provides its custodian/broker with payee-specific documentation (only IRS Forms W-8 and W-9; a disclosing QI cannot provide

documentary evidence for its account holders), in addition to a recipient-specific withholding statement (that includes income and proceeds), as well as the requisite Code Sec. 6031 nominee statement. (This new concept was previewed in the preamble to the final regulations for Code Sec. 1446(f) and the QI Rider.)

A disclosing QI is not required to provide the Code Sec. 6031 nominee statement to the QI’s nominee if such nominee maintains fully segregated and disclosed accounts for the disclosing QI’s account holders that include the information necessary for the PTP (or its agent) to issue a Schedule K-1 to each beneficial owner of the PTP interest. For these purposes, the term “nominee” includes “an entity ... that holds a PTP interest directly or indirectly for another person” and is not limited to nominees permitted to assume withholding on PTP distributions.

In addition, the 2023 QI Agreement incorporates the requirement of the QI Rider that a QI must act as a disclosing QI for the entire amount of a PTP distribution or amount realized from the sale of a PTP interest, commonly referred to as the “all or nothing” approach. The 2023 QI Agreement, however, clarifies that a QI may act as disclosing QI even if the Form W-8 associated with the payee account holder does not include a U.S. TIN. In other words, the lack of a U.S. TIN on a Form W-8 will no longer prevent a QI from acting as a disclosing QI for the entire amount of a payment made to multiple account holders due to any account holder failing to provide a U.S. TIN. The QI must nevertheless use its best efforts, as set forth under the 2023 QI Agreement and described above, to obtain a U.S. TIN for any such account holder.

In addition, the 2023 QI Agreement makes clear that a disclosing QI must disclose both its U.S. and non-U.S. account holders.

The 2023 QI Agreement retains the requirement that a disclosing QI provides a valid withholding certificate for each account holder (aside from the U.S. TIN requirement, discussed above). A disclosing QI may wish to discuss this requirement with its custodian/broker so that there is an understanding between the parties to promptly remediate any withholding certificate or withholding statement that is considered to be invalid by the custodian/broker.

### Certification Regarding Code Secs. 1446(a) and (f)

The 2023 QI Agreement adds a new certification regarding a QI’s procedures for complying with Code Secs. 1446(a)

and (f) and (more generally) that the QI has acted only to the extent permitted under the QI agreement. Thus, for example, a QI would not be able to make this certification if it represents its status as a QI with respect to an amount realized paid to an account holder for an interest in a partnership that is not a PTP.

To the extent an entity makes the decision to act as a QI with respect to Code Secs. 1446(a) and (f), it should carefully consider this new certification and ensure that it is not acting in a QI capacity with respect to an interest in a non-PTP. This may involve discussions with a QI's custodian/broker to ensure PTPs and non-PTPs are not held in the same account and are documented separately.

## Collective Refund Procedure for Purposes of Code Secs. 1446(a) and (f)

The 2023 QI Agreement provides that a QI is unable to apply the collective refund procedures for overwithholding under Code Secs. 1446(a) and (f). This is because account holders receiving payments subject to withholding under Code Sec. 1446(a) or (f) are required to file U.S. income tax returns to report these payments and should claim any associated credits or refunds of the withholding on such returns.

## Presumption Rules

The presumption rules that apply where a QI has undocumented account holders have been updated for purposes of Code Sec. 1446(a) by including a reference to the presumption rule of Reg. §1.1446-1(c)(3) for a QI to determine the status of a partner as a foreign individual or corporation (and, thus, the rate of withholding) when the QI cannot reliably associate a payment subject to Code Sec. 1446(a) withholding with valid documentation from a partner in cases that were not previously covered under the 2017 QI Agreement.

## QDDs and Qualified Security Lenders

The 2023 QI Agreement also describes the requirements for QIs acting as QDDs and the requirements of QIs regarding payments of dividend equivalents they receive in an intermediary capacity for purposes of regulations issued under Code Secs. 871(m), 1441, 1461, and 1473.

The QDD provisions in the 2023 QI Agreement are generally retained from the 2017 QI Agreement, with some added guidance for QDDs that are partnerships or a branch of a partnership and incorporate portions of prior FAQs that supplement the 2017 QI Agreement,

as well as certain transitional relief provided by Notice 2022-37.

A QDD must assume primary chapter 3 and chapter 4 withholding and reporting responsibility and primary Form 1099 reporting and backup withholding responsibility under Code Sec. 3406 for payments made as a QDD regarding potential Code Sec. 871(m) transactions.

A QI acting as a QDD generally remains liable for its QDD tax liability and must report that liability on the appropriate U.S. tax returns. While a QDD is not required to perform a periodic review for calendar years 2023 and 2024 regarding its QDD activities, the 2023 QI Agreement requires a QDD to certify, as part of its periodic certification, that it made a good-faith effort to comply with Code Sec. 871(m) regulations and the relevant provisions of the 2023 QI Agreement. The 2023 QI Agreement clarifies that in order to rely on the good-faith effort standard, a QI must provide the information previously specified by FAQ #19—Certifications and Periodic Reviews for the 2017 QI Agreement.<sup>6</sup> The requirements for QDD periodic certification reporting and a sample of QDD accounts are expected to be released in the future in the form of a rider to the 2023 QI Agreement.

For qualified security lenders (“QSLs”), a withholding agent may not act as a QSL for payments made after 2024. Until December 31, 2024, if a QI that is not acting as a QDD acts as a QSL, it must act as a QSL and assume primary withholding responsibility (including Form 1099 reporting) for all substitute dividends received and paid by the QI when acting as an intermediary or dealer regarding securities lending and similar transactions.

## Validity Standards for Documentation

FAQs# 1 and 2—Provisions for 2017 QI Agreement, which provide additional guidance on the standard certain QIs must apply when treating documentation provided by a direct account holder as unreliable, have been incorporated in the 2023 QI Agreement. First, a QI may treat a direct account holder's claim of non-U.S. status on a Form W-8 as unreliable only if the QI had a U.S. mailing or permanent address for the account holder (as opposed to having a U.S. mailing or permanent address in the account file). Second, with respect to a claim of treaty benefits, a QI is not required to redocument a direct account holder claiming treaty benefits if the QI had documented such an account holder before January 1, 2018, in accordance with the prior applicable

guidance. For those direct account holders documented on or after January 1, 2018, a QI should have a permanent residence address for the direct account holder in the jurisdiction associated with the documentation being relied upon.

The 2023 QI Agreement added cross-references to the specific provisions of the applicable Treasury Regulations and reorganizes section 5.10 with new subsections for easier reference. Section 5.10(A) now includes cross-references to regulations addressing general validity standards applicable to documentation for purposes of Code Secs. 1446(a) and (f).

## Curing Hold Mail Instructions

In 2020, the Treasury Department and the IRS published final regulations (T.D. 9890) that modified the hold mail rules, whereby a withholding agent may treat an account holder's address subject to a hold mail instruction as a permanent residence address if the withholding agent obtains documentary evidence that supports the person's claim of non-U.S. status or claim of residence in a treaty country (as applicable). These requirements are now incorporated in the 2023 QI Agreement, which clarifies when a QI may treat an address subject to a hold mail instruction as a permanent residence address.

## Furnishing Recipient-Specific IRS Form 1042-S to the Account Holder

The period of time that an account holder may request a recipient-specific Form 1042-S from the QI is now limited. Specifically, a non-U.S. account holder must make a written request for the form within two full calendar years following the year of the payment for which the form is requested. If, however, a QI files a Form 1042-S to report a payment subject to Code Sec. 1446(a) or (f) withholding with respect to an account holder that requests a Form 1042-S for the same calendar year, the account holder then has three calendar years from the year of the payment to make a written request for a recipient-specific Form 1042-S. When required, the QI must provide the account holder with a separate Form 1042-S for each amount reportable on Form 1042-S that was paid to the account holder for the calendar year (which facilitates the account holder's proper reporting of income paid by the QI on the account holder's U.S. tax return).

A QI is permitted to deny any such requests for a recipient-specific Form 1042-S if the account holder does not

provide the QI with its U.S. TIN. That said, the 2023 QI Agreement does not address the timing for a QI to amend its pooled Form 1042-S reporting. QIs should be mindful of reporting mismatches in relation to unreconciled amounts.

## Compliance Requirements and Periodic Reviews

With regards to a QI's certification process, the 2023 QI Agreement broadly retained the review steps and compliance requirements provided under the current QI agreement and added requirements for purposes of a QI's responsibilities under Code Secs. 1446(a) and (f). That said, there are several additions/changes to the certification process and periodic review, some of which are highlighted below:

- **New Appendix III.** The 2023 QI Agreement includes a new Appendix III, which is intended to assist the IRS in determining whether Forms 1042 and 1042-S were filed accurately by a QI for the years of a certification period not covered by a periodic review (or all such years if a waiver of the periodic review is requested). This Appendix requires QIs to provide, for each applicable year, certain information reported on Form 1042 and Forms 1042-S (including amended forms), by box and line, reconcile certain information included on the Forms 1042-S issued to the QI to the Form 1042 and Forms 1042-S filed by the QI (and between the Form 1042 and Forms 1042-S filed by the QI) and provide explanations for any identified variances. QIs will be required to upload a completed copy of Appendix III as part of their periodic certifications using the attachment feature in the Qualified Intermediary Application and Account Management System ("QAAMS").
- **Submission of the periodic review report.** QIs must submit a copy of their periodic review report with their periodic certification. (The 2017 QI Agreement does not require a QI to submit the periodic review report with its periodic certification absent an IRS request for the report.)
- **Remediation plan.** A QI must submit a qualified certification to complete the remediation plan (as detailed in Part II.B.3 of Appendix I) and submit this information with the certification.
- **Revisions to Appendix I.** The 2023 QI Agreement adds certain information requests to Appendix I regarding a QI's activities related to withholding under Code Secs. 1446(a) and (f). As previously

mentioned, the 2023 QI Agreement adds a new certification regarding a QI's procedures for complying with Code Secs. 1446(a) and (f) and (more generally) that the QI has acted only to the extent permitted under the QI agreement.

- **Final certification and periodic review for terminating QIs.** The 2017 QI Agreement requires a QI terminating its QI Agreement to submit a final certification within six months of the date of termination regardless of whether a periodic review has been completed for the portion of the certification period preceding termination. The 2023 QI Agreement provides that if a QI terminates its QI agreement in the final year of a certification period, the QI must submit a periodic review report covering one of the two years before the year of termination unless the QI is granted a waiver.
- **Merger or acquisition and combined periodic review.** If a QI (predecessor QI) merges into or is acquired by another QI that assumes the predecessor QI's obligations relating to the predecessor QI's QI agreement (successor QI), and the predecessor QI is required to submit a periodic review report due to its termination, the predecessor QI may satisfy this requirement through a combined periodic review. A combined periodic review is a review that covers one of the two years before the year of the predecessor QI's termination and that includes accounts of both the predecessor QI and the successor QI for purposes of specified review procedures relating to documentation and withholding. Notwithstanding the performance of a combined periodic review, the predecessor QI and the successor QI must make separate certifications for the period covered by the combined periodic review. There is a process, however, for a predecessor QI to obtain a six-month extension from the deadline to submit its final certification, provided that the request for extension indicates that it is being made due to the combined periodic review and is delivered to the IRS before the deadline for the final certification.

## Communications Under the 2023 QI Agreement

The 2023 QI Agreement allows written notices sent by QIs to the IRS to be either mailed *via* registered, first-class mail or emailed to the IRS at *lbi.fi.qiwpissues@irs.gov*. Furthermore, the 2023 QI Agreement specifically states that the IRS will send notices by secure email to

the QI's responsible officer and other contact persons designated by the QI. QIs should ensure their information on QAAMS, including the responsible officer and other contact persons, are current to avoid missing communications from the IRS.

## Public List of QIs

As part of the application or renewal process of a QI agreement, every QI will be required to consent to have its name, status as a QI, and QI employer identification number ("QI-EIN") disclosed on a publicly available list of QIs to be published by the IRS on its website. This will ensure that entities do not misrepresent themselves as a QI when providing a W-8IMY to a withholding agent. While the IRS has not yet issued guidance (in the 2023 QI Agreement or elsewhere) addressing standards of knowledge and an entity's claim of QI status, QIs (and other withholding agents) should consider whether it is appropriate to confirm an entity's claim of QI status against the published list (similar to the Global Intermediary Identification Number ("GIIN") verification process).

## Online Authentication

The IRS is in the process of transitioning QAAMS to a modernized sign-in system with applicable multi-factor authentication procedures. According to the IRS, beginning in the spring of 2023, all QAAMS users will be required to have completed the credentialing process with the applicable credential service provider and use the multi-factor authentication procedures to access QAAMS.

## Notice 2023-8, Additional Guidance Related to Transfers of Publicly Traded Partnership Interests Under Code Sec. 1446(f)

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The Notice addresses specified major topics with respect to a broker's withholding obligations for purposes of Code Sec. 1446(f) (transfers of interests in PTP by non-U.S. persons), including non-U.S.-traded PTP interests, reliance on late certifications, and short sales of PTP interests. In addition to its application to brokers, the Notice provides that a QI applying the provisions of the 2023 QI Agreement may also rely on specified provisions of the Notice.

## Non-U.S.-Traded Entities

The Treasury regulations promulgated under Code Sec. 1446(f) generally provide that withholding on the sale of a PTP interest is required unless such PTP issues a Qualified Notice that a withholding exception is applicable. In response to public comments regarding the challenges presented in identifying non-U.S. entities that are PTPs, the Notice provides that the Treasury Department and the IRS intend to issue proposed regulations to provide withholding relief to brokers on the sale of an interest in an entity that is organized outside of the United States and that trades solely on a non-U.S. established securities market or a non-U.S. secondary market (“non-U.S.-traded entity”).

This proposed amendment would allow a broker that effects a sale of an interest in a non-U.S.-traded entity to presume that the entity is not a PTP for U.S. tax purposes unless the broker has actual knowledge otherwise. Where a broker has actual knowledge that a non-U.S.-traded entity is a PTP for U.S. tax purposes, then such broker would be required to withhold under Code Sec. 1446(f) (unless the broker has a Qualified Notice confirming that an exception applies or the PTP interest holder is eligible for a reduced rate of withholding).

## Late Certifications

Unlike the Reg. §§1.1441 and 1.1471, the Treasury regulations promulgated under Code Sec. 1446(f) do not currently permit a broker to rely on late tax certifications (*e.g.*, tax certifications received after the date of payment) with respect to the imposition of withholding tax. The Notice provides that the Treasury Department and the IRS intend to issue proposed regulations that permit brokers to rely on late certifications for purposes of withholding under Code Secs. 1446(a) and 1446(f). These late certification rules will generally coordinate with the late documentation rules under Code Secs. 1441 and 1471. The Notice does not define the term “certification” when discussing these intended proposed regulations. It is not entirely clear whether future proposed regulations will apply to both IRS Forms W-8 and W-9.

## Short Sales of PTP Interests

The Notice provides that the Treasury Department and the IRS intend to issue proposed regulations to provide an exception to withholding under Code Sec. 1446(f) on a PTP short sale. This PTP short sale exception would apply to a PTP short sale effected by a broker on behalf of a taxpayer that obtained the PTP interest from another party (including the broker or a customer of the broker) for sale to market. No withholding would be required on the sale to market of the PTP interest or on the later transfer by the taxpayer of an identical PTP interest to the original PTP interest owner.

The PTP short sale exception will not apply in certain situations in which there may be gain arising from the PTP short sale that is subject to Code Sec. 864(c)(8), including where, on the date that the sale to market is entered on the books of the broker, (i) the taxpayer holds substantially identical property in an account with the broker or (ii) the broker has actual knowledge that the taxpayer holds substantially identical property in an account with another broker. In such cases, the taxpayer may realize gain from the delivery of such substantially identical property to the original PTP interest owner or from the constructive sale rules.

## Conclusion

Despite the previewing of many concepts that have been incorporated into the 2023 QI Agreement, QIs will be required to significantly update policies and procedures, as well as operational systems, to properly reflect the current QI regime. This can be quite an undertaking for QIs, and considerable thought should be given to such updates. In light of increased enforcement efforts by the IRS, QIs must ensure that they are up-to-date with all QI-related obligations, taking into account that many QIs' current certification period will end at the end of 2023, requiring the QI to make its certifications to the IRS in 2024. Furthermore, QIs must ensure that they timely renew their QI Agreement in order to have a January 1, 2023 effective date.

## ENDNOTES

<sup>1</sup> Pursuant to Reg. §1.1441-1(e)(5).

<sup>2</sup> Rev. Proc. 2017-15, IRB 2017-3, 437.

<sup>3</sup> The term “publicly traded partnership interest” means “an interest in a publicly traded partnership if the interest is publicly traded on an established securities market

or is readily tradable on a secondary market (or the substantial equivalent thereof).” Reg. §1.1446(f)-1(b)(5).

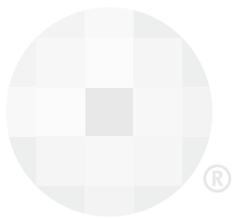
<sup>4</sup> Notice 2023-8, IRB 2023-2, 341, Section VI.

<sup>5</sup> These solicitation requirements are similar to those imposed on payors seeking missing TINs

on Forms 1099 and the establishment of reasonable cause under Reg. §301.6724-1(e).

<sup>6</sup> The FAQs referenced herein can be found at the following website: [www.irs.gov/businesses/corporations/qualified-intermediary-general-faqs](http://www.irs.gov/businesses/corporations/qualified-intermediary-general-faqs).

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