

# 2018: AN IMPORTANT YEAR FOR QI RESPONSIBLE OFFICERS

**The 2014 Qualified Intermediary Agreement ("QIA") replaced the previous external audit with an internal compliance and review program. As part of this program, the QI Responsible Officer ("RO") is required to certify to the IRS that the financial institution is compliant or not. In case of any material failure, the RO must ensure that corrective actions are taken.**

**Unless the QI benefits from a waiver, the RO must also designate a reviewer that meets certain qualifications to perform a periodic review.**

## CERTIFICATION OF INTERNAL CONTROLS

The QIA requires the RO to certify that the financial institution has implemented effective internal controls.

This applies even when the QI obtains a waiver of the periodic review.

In making this certification, the RO may rely on any processes, procedures, reviews, or certifications made by other persons that he determines are necessary to make the certification. This flexibility allows the RO to decide, for example, whether to hire an external party to conduct a review of the internal controls to ensure they are adequate.

The RO must document the procedures, processes, reviews, or certifications relied on in making his certification. Therefore, if the RO relies on internal or external reviewers, he must retain any report delivered by those reviewers.

When a QI has to perform a periodic review, the RO must take into account the results of this review when making his certification.

The QIA does not provide further prescriptive requirements about what process or documentation the RO must rely on to make the certification, because such prescriptive guidance would unnecessarily limit his discretion to structure a compliance program that, in his judgment, is necessary to make the certification.

A QI that is an FFI is also required to comply with FATCA requirements. The QIA clarified that the RO may rely on other persons with oversight or responsibility for FATCA compliance in making its compliance certifications. The QIA also specifies that in conducting the periodic review relating to FATCA compliance, the QI is only required to review the accounts for which it is acting as a QI.

For the certification period that ended in 2017, a QI that is a Qualified Derivative Dealer ("QDD") is not required to make the certification of internal controls as applicable to its QDD activities. It is rather required to certify that it had made a good-faith effort to comply with the relevant QDD provisions.

In case the RO identifies an event of default or a material failure that has not been corrected by the date of the certification, he cannot make a certification of effective internal controls. Instead, he must make a qualified certification.

For a QI with a QIA that has an effective date of June 30, 2014 through December 31, 2016, the initial certification period ended December 31, 2017. The certification is due at the IRS on or before September 1, 2018. However, for QIs that chose 2017 for their periodic review, the due date is March 1, 2019.

## PERIODIC REVIEW PROGRAM

The RO must in principle require a reviewer to test accounts related to the QI's documentation, withholding, reporting, and other obligations under the QIA, including its FATCA requirements. If there are deficiencies in meeting these obligations, the reviewer must identify them.

Under certain circumstances, a QI may apply for a waiver of the periodic review.

A QI is eligible to apply for a waiver if it meets these requirements:

1. The QI is an FFI that is not also acting as a QDD;
2. The QI is not part of a consolidated compliance program;

3. For each calendar year covered by the certification period, the reportable amounts received by the QI do not exceed \$5 million;
4. The QI has filed on time its Forms 1042, 1042-S, 945, 1099, and 8966, as applicable, for all calendar years covered by the certification period;
5. The QI has made the periodic certifications and reviews required as well as all certifications required pursuant to the QI's FATCA requirements;
6. The QI has made the certification of effective internal controls.

The QI must request the waiver at the time the RO makes its certification of effective internal controls.

The application for such a waiver must be specifically approved by the IRS; waiver applications are not approved automatically.

When a QI applies for a waiver, it is required to provide certain factual information along with its periodic certification (as specified in Parts I and III of Appendix I of the QI Agreement).

A QI which does not benefit from a waiver may use either an internal or an external reviewer to conduct the review. Whether the reviewer is an internal or external reviewer, the reviewer must have sufficient independence to objectively conduct the review and he cannot review his own work (for example, systems that the reviewer designed, or documentation that the reviewer validated in assisting a QI in its account-opening processes). To maintain an appropriate level of independence and integrity, reviewers cannot be reviewing their own work and should be in a position to make a negative assessment of the practices and procedures without concern about any negative impact for themselves.

Even though the QIA does not contain comprehensive rules regarding what constitutes independence, the

independence standard, as applied to external reviewers, is not applied on an individual or team basis but is applied on a company or firm-wide basis, when the firm has developed or assisted in the development of QI or FATCA policies or procedures. Therefore, the external reviewer cannot be reviewing systems, policies, or procedures, or the result thereof, that he or his firm was involved in designing, implementing or maintaining.

Moreover, a reviewer must have enough knowledge and experience to conduct the required review.

The results of the periodic review must be documented in a written report addressed to the RO, and the report must be available to the IRS upon request (with a certified translation into English if the report is not in English).

## UNDERWITHHOLDING

When a reviewer determines an amount of underwithholding, the QI has to pay the amount determined and has to report both the underwithholding determined by the review and any amount of underwithholding that was cured following the review. This applies to underwithholding for which valid documentation to support a reduced rate of withholding applied by the QI was obtained after the selection of the sample.

The 2017 QIA provided that a QI will pay any underwithheld tax without regard to projection. The IRS will determine if a projection of any underwithholding from a sample is required at the time the IRS reviews the QI's periodic certification.

## QDD REVIEW

For calendar year 2017, a QI that is a QDD is not required to perform a periodic review with respect to its QDD activities.

## CERTIFICATION ON IRS PORTAL

The IRS has announced that the QI application and account management system will be available to accept QI certifications beginning early April.

## HOW BDO CAN HELP

BDO can help the RO determine the scope of the tests to perform to support the internal controls certification.

BDO can also perform those tests whose results will be contained in a report addressed to the RO.

When the QI has to perform a review, BDO can perform the review based on an established methodology. BDO can also perform the reconciliation of the 1042-S reporting. The results of the review and reconciliation can be included in a report addressed to the RO.

BDO has developed an approach that will help the RO make the required certification based on reliable information.

In case the RO would need help to answer the certification questions, BDO would be pleased to assist.

## KEY CONTACTS



**Gerdy Roose**  
Tax Partner  
+352 45 123 371  
gerdy.roose@bdo.lu



**Sylvie Maestri**  
Operational Tax Director  
+352 45 123 589  
sylvie.maestri@bdo.lu

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