

Revocation of Qualified Intermediary Branch Rule

Notice 2006-35

SECTION 1. PURPOSE

This notice modifies Announcement 2000-48, 2000-1 C.B. 1243, and Notice 2001-43, 2001-2 C.B. 72, by providing that, generally, a branch of a financial institution may not act as a qualified intermediary (QI) after December 31, 2006, in a country that does not have approved know-your-customer (KYC) rules.

SECTION 2. BACKGROUND

Treasury regulation §1.1441-1(e)(5) permits a QI, as defined therein, to furnish a withholding certificate to a withholding agent on behalf of other persons for purposes of claiming and verifying reduced rates of withholding under section 1441 or 1442. To qualify as a QI, the intermediary must enter into a withholding agreement with the IRS, pursuant to §1.1441-1(e)(5)(iii), the terms of which are contained in Rev. Proc. 2000-12, 2000-1 C.B. 387 (QI Agreement). Rev. Proc. 2000-12 states that the IRS will not enter into a QI agreement that provides for the use of documentary evidence obtained under a country's KYC rules unless it has received certain information that allows it to determine whether those KYC rules are acceptable. Once the IRS determines that a country's KYC rules are acceptable, it lists such country as an approved jurisdiction on the IRS website. KYC rules relate to the capacity of a financial institution to determine whether their customers are U.S. persons and, if their customers are non-U.S. persons claiming the benefits of an income tax treaty, whether those customers are residents of the applicable treaty country. See Notice 2001-4, 2001-1 C.B. 267.

Announcement 2000-48 limits eligibility for QI status to financial entities organized in jurisdictions with approved KYC rules. However, Announcement 2000-48 (as modified by Notice 2001-43) permits a branch of a financial institution (but not a separate juridical entity affiliated with the financial institution) to act as a QI in a jurisdiction that does not have KYC rules, has unacceptable KYC rules, or has KYC rules awaiting IRS approval, if the branch is part of an entity organized in a country that does have acceptable KYC rules and the entity agrees to apply its home country KYC rules to the branch.

When the QI system was implemented, only a small number of jurisdictions had KYC rules that had been reviewed and approved by the IRS. In an effort to implement the QI system as quickly and broadly as possible, branches of financial entities were allowed to participate in the QI system under the standards of Announcement 2000-48 and Notice 2001-43.

Now that Treasury and the IRS have reviewed the KYC rules for all of the countries that submitted their KYC rules for review, and have approved the KYC rules of 57

countries, Treasury and the IRS believe that it is no longer prudent to permit branches of financial entities to operate as QIs in countries that do not have approved KYC rules. KYC rules are most effective when applied to the countries for which they were drafted. Further, because the QI system is largely self-regulated, it is appropriate to limit participation in the system to circumstances in which Treasury and the IRS have the greatest confidence that such self-regulation will be effective. A country's continuing lack of an acceptable set of KYC rules raises concerns about the effectiveness of self-regulation in that country.

SECTION 3. BRANCHES LOCATED OUTSIDE OF APPROVED KYC COUNTRIES

Branches of financial institutions will not be permitted to operate as QIs after December 31, 2006, if they are located outside of countries listed as having approved KYC rules on the IRS website at www.irs.ustreas.gov. However, branches of a financial institution that are operating as QIs under Announcement 2000-48 (as modified by Notice 2001-43) on April 3, 2006, may continue to operate as QIs through December 31, 2007, provided that (1) the financial institution mails a written request for an extension, on or before June 30, 2006, to:

KYC Coordinator
Internal Revenue Service
290 Broadway, 12th Floor
New York, New York 10007

(2) the request identifies the jurisdictions in which such branches are located and briefly describes what steps those jurisdictions have taken to implement KYC rules; and (3) the request is approved, in writing, by the KYC Coordinator.

Branches of financial institutions that operate in non-KYC approved jurisdictions will be required to act as non-qualified intermediaries after December 31, 2006, or after December 31, 2007, as applicable.

SECTION 4. EFFECT ON OTHER DOCUMENTS

This notice modifies Announcement 2000-48 and Notice 2001-43.

SECTION 5. CONTACT INFORMATION

The principle authors of this notice are Jason Kleinman and Ethan Atticks of the Office of the Associate Chief Counsel (International). For further information regarding this notice, contact Jason Kleinman or Ethan Atticks at (202) 622-3840 (not a toll-free call).