

871(m) Qualified Indices Data

Background

Amendments to the US Internal Revenue Service (IRS) regulations 871(m) announced in September 2015 came into effect January 1, 2017. These changes require dealers to withhold US federal taxes on certain equity linked instruments, including those which reference indices. IRS guidance notes published on December 2 2016 provide further details on enforcement and administration during the phase in period.

In order to comply with these changes dealers must be able to identify which equity linked instruments are in scope and as part of that determination the IRS has provided a set of criteria for qualified and non-qualified indices as part of 871(m).

Identifying Qualified Indices

Analysis to identify qualified and non-qualified indices are made on the first business day of every year. This determination applies to all derivatives based on the index throughout the year.

The criteria are designed to qualify indices which are passive, diverse and widely used.

- Reference 25 or more securities
- Reference primarily long positions
- No “underlying” security can represent more than 15% of the weighting
- Five or fewer “underlying” securities cannot represent more than 40% of the weighting
- U.S. dividend yield \leq 1.5x the dividend yield of last year’s S&P 500 Index
- Is modified or rebalanced only according to publicly stated, predefined criteria
- Traded through futures or option contracts on IRS- recognized exchanges

There is also an alternative qualification test for indices that may not meet the above criteria but contain 10% or fewer U.S. underlying components.

Exchange Data International Solution

Exchange Data International (EDI) has reviewed the universe of underlying indices for derivatives traded on the full list of exchanges recognised by the IRS.

Index composition, weightings, dividend yields, and rebalancing methodologies for each are analysed against the IRS 871(m) qualified indices definitions allowing each index to be appropriately flagged. Coverage is for indices traded on the recognized exchanges and does not utilize the alternative 10% criteria.

EDI can provide a full list of the over 200 indices which fall within scope of 871(m) providing these fields:

- Qualified / Not Qualified Indicator
- Ticker/Symbol
- ISIN
- Bloomberg Code
- Index Name
- Index Provider
- Exchange where options/futures are traded
- Greater than 25 securities indicator
- No “underlying” security $>$ 15% indicator
- Top 5 “underlying” securities not $>$ 40% indicator
- Dividend yield \leq 1.5x the dividend yield of last year’s S&P 500 Index indicator

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