

U.S. income tax withholding and 'beneficial ownership'

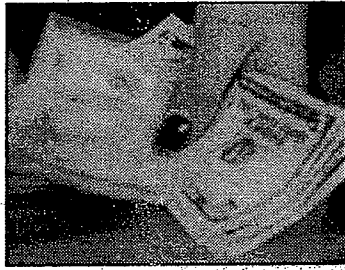
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Most payments of United States source fixed or determinable annual or periodical gains, profits, and income (e.g. dividends or rental income) to a foreign person are subject to a 30 percent tax imposed on the gross amount so long as such income is not attributable to a U.S. trade or business of such foreign person.

The Internal Revenue Code makes exceptions for investment-type interest (e.g., interest on bank deposits and treasury or corporate bonds) and most capital gains. In addition, U.S. tax treaties typically reduce or eliminate the 30 percent tax.

When applicable, the tax is collected by way of withholding on the amount paid. Where the tax liability is satisfied at source, a foreign taxpayer is generally not required to file a U.S. income tax return with the Internal Revenue Service

(IRS). Instead, information about the payment and any amount withheld is reported to the IRS by the payor of the income, the withholding agent, who makes an annual return (on Form 1042) for the total



amounts withheld during the calendar year. The withholding agent must also file a Form 1042-S with the IRS, reporting the total amounts paid to each beneficial owner during the year, and must furnish a copy of such form to the beneficial owner. A withholding agent is personally liable for any tax required to be withheld.

RULES

Under current rules, a foreign person must provide a

Form W-8 (various types of which are discussed below) to a U.S. payor as evidence of its foreign status. A payor making a payment to a foreign person may generally rely on such statement to reduce the rate of withholding, when applicable.

Form W-8BEN (Certificate of Foreign Status of Beneficial Owner for United States

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Withholding) would be provided to a withholding agent or payor by a beneficial owner of certain types of income to establish foreign status, to claim that such person is the beneficial owner of the income for which the form is being furnished, and if applicable, to claim a reduced rate of, or exemption from, withholding as a resident of a foreign country with which the U.S. has an income tax treaty.

Form W-8IMY (Certificate of Foreign Intermediary, Foreign Partnership, and Certain U.S. Branches for United States Tax Withholding) would be provided to a withholding agent or payor by a foreign intermediary, foreign partnership, and certain U.S. branches, either to make representations regarding the status of beneficial owners of the amount paid or to transmit appropriate documentation to the withholding agent.

SPECIAL

There are special rules regarding the application of treaty benefits for "hybrid" entities (i.e., entities that are considered corporate entities under the laws of one treaty jurisdiction and "fiscally transparent" entities under the laws of another treaty jurisdiction). In general, though, the "beneficial owner" of the income of a corporate entity, the owner who is required to provide Form W-8BEN, should be the entity itself and not the shareholders.

"Beneficial owner" for these purposes is defined as the "person who is the owner of the income for tax purposes

and who beneficially owns that income. A person shall be treated as the owner of the income to the extent that it is required under U.S. tax principles to include the amount paid in gross income..."

As the certification rules discussed above are relatively new (the last regulations in this area were substantially amended in 2000 and, as discussed below, additional amendments are anticipated), confusion oftentimes leads to U.S. financial institutions and other payors requesting unnecessary information of payees. For example, some payors request information regarding the shareholders of a corporate entity. However, as discussed above, in most cases, the beneficial owner should be the corporate entity and not its shareholders.

This is an area of the U.S. tax law which leads to great confusion amongst foreign individuals, U.S. financial institutions, and the IRS. Due to these compliance challenges, the IRS continues to increase its focus in this area and plans to issue proposed regulations in the next several months that will outline a process of checking Forms W-8 against a third-party database from credit rating agencies, banks, financial institutions, and other public and private sources, in an effort to increase compliance.

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