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United States

Tax Treaty Updates – New treaty protocols ratified by Senate

What is the Update?

After a delay of almost nine years, the Senate has now approved four new treaties/protocols with Spain, Switzerland, Japan and Luxembourg. The new treaties/protocols address various topics, including withholding taxes on transactions between US and foreign companies, and taxation of both individual and corporate taxpayers to avoid double tax situations. Each country protocol deals with amendments to a few or several articles within the tax treaty, however, all include an amendment to the article related to the "Exchange of Information" between the US tax authorities and other countries, which has been the major reason for holding up the protocols. Some of the additional changes to the articles address reducing withholdings and/or assist in resolving tax disputes. More specifically –

a. **Spain** – The Spain protocol includes amendments to several articles of the treaty including a focus on investment income of Dividends, Interest, Royalties, and Capital Gains, Limitation on Benefits, and Pensions. The update to the pension provision will be impactful to international employees to avoid a double tax situation.

The Spain protocol will enter into force three months following the date the US and Spain notify each other that their respective ratification procedures have been satisfied.

b. **Luxembourg** – The protocol amendments for Luxembourg relate to the Exchange of Information article, updating how information may be obtained, who is required to provide information and how it may be used. The Luxembourg protocol will enter into force on the date the US and Luxembourg notify each other in writing that their respective ratification procedures have been satisfied and would have effect for exchange of information requests made on or after the date the protocol enters into force with regard to tax years beginning on or after January 1, 2009.

c. **Japan** – Similar to Spain, the Japan protocol includes amendments to several of the treaty articles including Residency, Interest, Real Property, Gains, Directors' Fees, Mutual Agreement Procedure, Exchange of Information and others to be deleted. It would require the Japanese and US revenue authorities to give limited assistance to one another in the collection of taxes. This protocol will enter into force on the date the US and Japan exchange instruments of ratification.

d. **Switzerland** – The protocol amendments for Switzerland include Dividends, Mutual Agreement Procedure and Exchange of Information. The treaty also prohibits banks from denying a request for information relevant to stop tax evasion. The protocol will enter into force upon the exchange of instruments of ratification by the US and Swiss governments.

The ratification of the four tax protocols by the Senate on July 16 and July 17, 2019 details which country has the authority to tax which income to avoid having individual taxpayers paying taxes both in the country where they are working and their home country. These protocols are intended to make the U.S. a more attractive place for companies in these countries to do business and increase activity of global mobility programs.

Further updates anticipated:

In addition to the tax protocols, there are also three other income tax treaties with Chile, Hungary and Poland that are still awaiting consideration by the Senate Foreign Relations Committee. According to the Treasury, each of these treaties will require modifications to reflect changes made under the Tax Cuts and Jobs Act, however, there is still momentum to move these treaties forward for approval this calendar year.

The Hungary and Poland income tax treaties have been effective since 1979 and 1974, respectively, and the pending treaties would include significant changes to bring them into conformity with modern U.S. tax treaty policy. In relation to Hungary, Article 2 has been updated to broaden the types of taxes covered under the treaty. Additional changes relate to residency and an expansion of the details on business profits, dividends, interest and capital gains. The treaty also added a few new articles for associated enterprises, directors' fees, entertainers and sportsmen, pensions and income from social security and limitations on benefits.

The Poland treaty expands the article on general scope as well as the details related to residency. Similar to the Hungarian treaty, the Poland treaty also expands the articles related to dividends, interest, capital gains and new articles were added for branch profits, directors' fees, entertainers and sportsmen, pensions/social security/annuities/alimony/child support, other income, and limitations on benefits.

In relation to Chile, this tax treaty would be the first implemented between the US and Chile. The treaty details primarily follow the US treaty model, with a few adjustments to some articles including an additional article specifically related to the taxation of Capital represented by real property.

Should these treaties be approved, this would be a benefit to individuals who may be eligible to be taxed at a reduced rate or exempt from U.S. income taxes on certain items of income they received. Continue to watch for further developments this year.

Background

As tax treaties are negotiated between the US and other countries, both countries must ratify the treaty for it to be approved. In the US, the approval process requires the US Senate to vote to approve the treaty, followed by ratification by the President. While social security treaties, commonly referred to as Totalization Agreements, have been approved by the Senate, new income tax treaties have been on hold since 2011 due to concerns in the Senate on information disclosure provisions within the treaties/protocols.

Deloitte's view

As mentioned, ratification of these income tax treaties has been on hold for many years. With this recent action by the Senate, there is momentum for further ratification of treaties going forward. This

will likely impact how multi-national companies manage their international businesses and how they manage their international assignee populations. When planning for an assignment, careful review of an applicable treaty should be completed to reduce potential costs related to the assignment.