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MEMORANDUM FOR

FROM: Philip Garlett  
Senior Technical Reviewer, Branch 2

SUBJECT: **U.K. Supplemental Withholding**

This memorandum responds to your letter dated January 12, 2000, requesting advise on the imposition of supplemental withholding after December 31, 2000. Your letter was forwarded to this office by John Manton from the Office of Assistant Commissioner (International) ("ACI").

**Issue:**

1. What is the effective date of the final withholding regulations?
2. Should United Kingdom ("U.K.") intermediaries continue to impose supplemental withholding on payments to account holders in non-treaty countries after the effective date of the final withholding regulations?
3. Under the new withholding regime, should U.K. Inland Revenue cease to play any role in collecting additional U.S. tax, *i.e.*, the responsibility will fall on qualified intermediaries?

**Discussion:**

**1. What is the effective date of the final withholding regulations?**

On October 14, 1997, the Department of the Treasury and the Internal Revenue Service ("the IRS") issued final Income Tax Regulations (the "final withholding regulations") governing withholding on payments of U.S. source income to foreign persons. Those regulations were published in the Federal Register as T.D. 8734. As announced in T.D. 8856 (64 FR 73408), the regulations apply to payments made after December 31, 2000.

**2. Should U.K. intermediaries continue to impose supplemental withholding on payments to account holders in non-treaty countries after the effective date of the final withholding regulations?**

The final withholding regulations eliminate the current “address rule” for withholding on dividends at reduced rates under a treaty. Under the address rule, the beneficial owner is not required to certify its entitlement to treaty benefits to obtain a reduced rate of withholding at source under an income-tax treaty. Instead, the withholding agent looks to the address of the recipient and withholds at the rate applicable to the recipient.

Under the address rule, if a payment of dividends is made by a U.S. withholding agent to an entity with an address in the U.K., the withholding agent is required to withhold only 15%. Under the supplemental withholding regime, if the U.K. entity has an account holder in a non-treaty country, the entity withholds and remits to the U.K. Inland Revenue an additional 15% tax at the time the payment is made. In turn, the Inland Revenue periodically forwards such payments to the Philadelphia Service Center. The Inland Revenue provides the dividend recipient and U.K. payor information to ACI on Form 3206 several times a year.

The final withholding regulations eliminate the “address rule” for dividends and instead require a treaty claimant to establish its entitlement to a reduced rate of withholding with a withholding agent (whether a U.S. withholding agent or a qualified intermediary). If the withholding agent does not have the required documentation to establish a reduced rate, it must withhold at the full 30% rate. Because entitlement to treaty benefits must be established with a withholding agent before the dividend is paid, it is not necessary for U.K. entities to impose supplemental withholding on payments to account holders in non-treaty countries after the final withholding regulations become effective. Further, once the final withholding regulations are in effect, the requirement to supply AC(I) with Forms 3206 is also eliminated. However, until January 1, 2001, U.K. intermediaries should continue supplemental withholding on payments to account holders in non-treaty countries.

**3. Under the new withholding regime, should U.K. Inland Revenue cease to play any role in collecting additional U.S. tax, *i.e.*, the responsibility will fall on qualified intermediaries?**

There will be no need for U.K. Inland Revenue to continue its supplemental withholding procedures under the new withholding regulations. For this purpose, it is not relevant whether a particular U.K. institution is a qualified intermediary or a nonqualified intermediary. The U.S. will, however, continue to look to the United Kingdom’s continuing assistance in other respects pursuant to Article 26(2) of the U.S.-U.K. Income tax treaty.

Philip Garlett  
Senior Technical Reviewer, Branch 2