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AN ALERT FROM THE BDO INTERNATIONAL TAX PRACTICE

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SUBJECT

NEW PROTOCOL TO UNITED STATES – FRANCE INCOME TAX TREATY ENTERS INTO FORCE CREATING POSSIBLE REFUND OPPORTUNITY FOR CERTAIN DIVIDEND AND ROYALTY PAYMENTS

SUMMARY

A potential refund opportunity exists for excess withholding tax on dividends and royalties as a result of the entry into force of the United States – France Treaty Protocol (the "Protocol")[1] for payments made and taxes withheld in 2009.

AFFECTING

United States and French companies that qualify for the zero-percent withholding rate on intercompany dividends from French or United States subsidiaries and royalty payments.

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[1] Convention between the Government of the United States of America and the Government of the French Republic for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, signed at Paris on August 31, 1994, as amended by the Protocol signed on December 8, 2004.

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BACKGROUND

The Protocol between the United States and France, which had been signed on January 13, 2009, entered into force upon the exchange of instruments of ratification between the United States and France on December 23, 2009. See our earlier (February 2009) alert at http://www.bdo.com/download.aspx?id=977 for a more complete discussion of specific provisions of the Protocol.

CHANGES IN WITHHOLDING TAX ON CERTAIN DIVIDENDS AND ROYALTIES

The Protocol reduces withholding tax rates on certain dividends and royalty payments to qualified residents.

Dividends

The Protocol includes a zero rate of withholding tax on dividends paid to a corporate owner. In order to qualify for the zero-percent withholding tax rate on cross-border dividends, the company receiving the dividends must own at least 80 percent, directly or indirectly, of the voting stock of the dividend-paying company if resident of the United States; and 80 percent of the capital of the dividend-paying company if resident of France, and the company must otherwise be eligible for treaty benefits under the Limitation on Benefits clause. The ownership requirement must be met for a period of at least 12 months ending on the date on which the entitlement of the dividends is determined.

A five-percent withholding rate applies when the dividend-receiving company owns directly at least ten percent of the voting stock of the dividend paying company and is resident in the United States. If the dividend-paying company is a resident of France, then the beneficial owner of the dividends must own directly or indirectly at least 10 percent of the capital of that company.

A 15-percent withholding rate on dividends paid to qualified residents will apply in all other cases.

Royalties

Withholding tax on cross-border royalties is eliminated under the Protocol so that royalties may only be taxed in the resident country of the beneficial owner of the royalties unless the beneficial owner has a permanent establishment or fixed base in the source country.

REFUND PROCEDURES

United States Withholding (French Taxpayer)

A United States subsidiary that withheld more than what is now required under the Protocol and made a deposit of the withheld tax may be eligible to adjust the over-withheld amount under either a reimbursement procedure or a set-off procedure. Reimbursement adjustments must be made before the end of the calendar year following the calendar year of the excess withholding. A set-off is available until the earlier of either the due date of Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding, for the calendar year of the excess withholding or the date Form 1042-S was actually filed with the Service. Thereafter, a refund of the amount of the excess withholding can only be claimed by the French parent by filing a United States income tax return (Form 1120-F, U.S. Income Tax Return of a Foreign Corporation, for a corporate payee). In order to benefit from the zero-percent withholding rate, a new Form W-8BEN, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding, should be completed by the French parent company and provided to the respective withholding agent (the United States subsidiary) accounting for the change in circumstances.

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French Withholding (United States Taxpayer)

Currently, the French tax administration has not published specific procedures on how to obtain a refund for the excess withholding in France. However, the refund procedure should be similar to the general refund claims previously made under the prior treaty protocol. The beneficial owner of the dividend (the United States parent) should provide a Certificate of United States Residency and additional certification verifying that the beneficial owner is eligible for the withholding tax exemption under the new Protocol with the request for the refund of any excess withheld tax.

The tax refund procedure in France is similar to a general refund claim, by which the taxpayer requests a benefit of the double tax treaty provision by completing two forms: (1) a residence certificate, Form 5000, which was previously submitted to the foreign document certification unit of the IRS (via Form 6166), and (2) an application for the benefit of reduced withholding tax rate on dividends (Form 5001) or royalties (Form 5003). The certificate of residence must be fulfilled in triplicate, with two English and one French language copies. The paying entity, which paid the dividend and the corresponding withholding taxes must send a refund claim (simple letter) to the non-resident tax office, with Forms 5000 and 5001/5003 including its bank details for refund.

▶ ENTRY INTO FORCE

Several provisions (including withholding taxes withheld at the source) under the Protocol are effective for the year of the entry into force of the Protocol. This effective date may provide certain taxpayers the ability to claim a refund of excess withholding tax on dividends and royalties paid in 2009.

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