

Newsalert

International Tax Services

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Japan

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PwC International Tax Services Network

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U.S. Asia Pacific Tax Group

The Asia Pacific Tax Group ("APTG") prepared this news alert. The APTG is part of PwC International Tax Services in the U.S. The group includes people from overseas offices of PwC – giving it a powerful knowledge base to solve Asia Pacific tax issues and optimize global tax rates. If you would like to contact a member of APTG please speak to Margaret Milcetic at (646) 394 4711.

For issues relating to this news alert please contact your local international tax services advisor or the specialists listed at the end of this article.

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Japan and the U.S. Introduce New Procedural Requirements For Eliminating / Reducing Withholding Tax Rates Under The New U.S.- Japan Income Tax Treaty

The new U.S.-Japan income tax treaty provides for the elimination or reduction of withholding taxes on dividends, interest, and royalties paid or accrued on or after July 1, 2004. However, the Japanese Tax Authorities will not automatically respect these new withholding tax rates on payments to U.S. residents. U.S. Taxpayers must satisfy certain procedural requirements and provide specified information to the Japanese Payor, which must then be filed with the Tax Authorities by the Payor prior to payment, in order for the Treaty withholding tax rates to apply.

Specifically, in order to receive the benefit of the reduced rates of withholding under the new treaty, Japan will require that:

- A U.S. Recipient of dividends must file Form 1, "Application Form For Income Tax Convention (Relief from Japanese Income Tax on Dividends)";
- A U.S. Recipient of interest must file Form 2, "Application Form For Income Tax Convention (Relief from Japanese Income Tax on Interest)"; and
- A U.S. Recipient of royalties must file Form 3, "Application Form For Income Tax Convention (Relief from Japanese Income Tax on Royalties)".

Each form is required to be prepared in duplicate for each Payor of a dividend, interest or royalty payment, and provided to the Payor. The original is filed, by the Payor, with the District Director of the Tax Office in the district where the Payor resides on the day before the payment is made.

In addition, Forms 1, 2, and 3 will require the following attachments:

- Form 17, "Attachment Form For Limitation On Benefits Article";
- Form 16, "List of the Member of Foreign Company", this form is required in the case that members/shareholders of a foreign corporation claim treaty benefits (e.g., an LLC which has elected U.S. tax treatment as a partnership or disregarded entity) and;
- In the case of royalties, the attachment of the licensing agreement.

Further, Forms 1, 2, and 3, must be filed with a U.S. residency certification, Form 6166, "Certification of Filing a Tax Return", issued by the IRS. Note that the Japanese Tax Authorities will require an original Form 6166 to be attached to Form 17, not a copy. Therefore, especially in the case where the treaty rate is zero, the submission package should include Forms 1, 2 and/or 3, together with Form 17 and an original Form 6166.

To receive a Form 6166, U.S. taxpayers should apply for current and/or prior year certification of U.S. residency by filing the newly issued Form 8802, "Application for United States Residency Certification" at least 30 days prior to the date the taxpayer requires the certification.

Instructions applicable to the new U.S. tax certification under new Form 8802 were issued by the Internal Revenue Service in IR-2004-78 on June 8, 2004. Although mandatory use of Form 8802 is not effective until July 5, 2004, the IRS will accept and process the new form immediately. If an entity is eligible for U.S. residency certification, the IRS will issue Form 6166.

U.S. recipients of Japanese sourced dividend, interest, and royalty payments must design and implement new compliance procedures to comply proactively with the new U.S. and Japanese forms and pre-payment filing requirements for reduced rates of withholding tax. Failure of the Payor to file the above-mentioned forms with the District Director of the Tax office and to complete these procedures on a timely basis in advance of scheduled payments, will require the Japanese Payor to withhold at the domestic withholding tax rate of 20 percent, notwithstanding technical eligibility for a 0% treaty rate. (Further, a US Payee must then request the Japanese Payor to make the necessary applications for a refund of any excess withholding taxes collected on its behalf, as the US Payee is itself not a recognized taxpayer in Japan.)

Additional guidance from the IRS and the NTA relating to the application of the new treaty is now available through a press release issued by The Department of the Treasury (JS-1737) on June 23, 2004:

<http://www.treas.gov/press/releases/js1737.htm>

For more detailed information, please do not hesitate to contact

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