Client Alert
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US Senate Ratifies Protocols to US Tax Treaties with Japan, Luxembourg, Spain, and Switzerland

On August 6, 2019, President Donald Trump signed instruments of ratification of Protocols amending four bilateral tax double taxation treaties ("DTTs") between the United States and each of Japan, Luxembourg, Spain, and Switzerland. The four Protocols were negotiated nearly a decade ago under the Obama administration, but the US Senate only approved ratification in late July of this year. The Protocols enter into force on the date upon which the United States and the relevant Contracting State exchange instruments of ratification. However, in the United States, ratification was not considered complete until the President signed the instrument of ratification, which was drafted after the US Senate voted to ratify the Protocols.

The Protocols will modernize the treaties with Japan, Luxembourg, Spain, and Switzerland in various areas but predominately in the mutual support and coordination of government efforts to address tax evasion. The Protocols also harmonize the treaties with the underlying international network of US DTTs, as well as with the OECD's efforts to coordinate the reform of international taxation. This client alert will provide a high-level summary of the changes brought about by the recently passed Protocols and will highlight key points relevant for interested stakeholders.

Amended Tax Treaties with Japan, Luxembourg, Spain, and Switzerland – What's Changed?

Japan

The Protocol (the "Japan Protocol") Amending the Convention Between the Government of United States of America and the Government of Japan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (the "US-Japan DTT") was signed on January 24, 2013, and submitted to the US Senate for advice and consent on April 13, 2015. As with the other recently-ratified Protocols, the Japan Protocol has languished in the US Senate for several years.

The Protocol amends the US-Japan DTT, which was concluded in 2003 and which replaced a 1971 treaty. Though the US-Japan DTT already included many of the modern provisions of the US model income tax treaty, the Japan Protocol inserts two of the most recently developed aspects of US tax treaties: mandatory binding arbitration and the exchange of information. Many of the other amendments made under the Japan Protocol are attributable to changes in US and Japanese domestic law.

Residency

The Japan Protocol amends the residency article to address dual-resident persons (other than individuals). If a person other than an individual is resident in both the United States and Japan, that person is not considered a "resident" of either Contracting State for purposes of the Convention. A dual-resident entity may still claim benefits under the US-Japan DTT that are not limited to "residents", such as the mandate in Article 24 that neither the United States nor Japan can impose discriminatory taxation on "nationals" of the other Contracting State. This provision does not affect the ability to claim treaty benefits for payments made by the dual-resident entity.

Dividends

The Japan Protocol amended the dividends article to modify the required ownership to qualify for an exemption from withholding. Under the Japan Protocol, the recipient must own at least 50 percent of the voting stock of the payor to qualify for the exemption, while the existing US-Japan DTT required that the recipient own more than 50 percent. The Japan Protocol also shortens the holding period requirement from 12 to six months prior to the date on which entitlement to the dividend is determined.

Interest

The Japan Protocol replaces the existing article on interest, which generally allowed for a 10% withholding tax, to include a new provision that generally provides for a zero rate of withholding in the source country. Under the new provision, the state of residence of a beneficial owner of an interest payment is generally granted the exclusive right to tax that interest payment.

The new interest article provides two exceptions to the residency-country general rule, one with respect to contingent interest, which remains subject to a 10% withholding tax, and the second for certain amounts derived with respect to REMICs, which remains subject to tax in accordance with the Contracting State's domestic law. Contingent interest is determined by reference to the receipts, sales, income, profits or other cash flow of the debtor or a related person, to any change in the value of any property of the debtor or a related person or to any dividend, partnership distribution or similar payment made by the debtor or a related person, or any other interest similar to such interest. The new interest article also retains the existing exception for when the beneficial owner of the interest carries on business through a permanent establishment in the country in which the interest arises.

The new interest article retains the existing sourcing rule. Interest generally is considered to arise in the country in which the payor is resident. The new interest article also retains the existing anti-conduit rule as well as the definition of the term "interest". Interest is defined as "income from debt claims of every kind, whether or not secured by a mortgage and whether or not carrying a right to participate in the debtor's profits". The term also includes amounts subject to the same tax treatment as income from money lent under the laws of the country in which the income arises, meaning that US definitions of interest apply. The

Technical Explanation to the Japan Protocol (the "Japan Technical Explanation") references sections 1273, 482, 1286, 7872, 702, and 860E of the US Internal Revenue Code (the "Code"), among other provisions. This portion of the Japan Technical Explanation does not appear to have been updated to reflect the proposed, but yet-to-be-finalized, regulations under section 163(j), which include an expansive definition of "interest"

Real Property

The Japan Protocol also modifies the definition of "real property" in Article 13 of the US-Japan DTT, relating to taxation of gains from the alienation of property. The new definition includes (1) real property referred to in Article 6, i.e., a direct interest in the property situated in a Contracting State, (2) where the real property is located in Japan, shares or interest in a company, partnership, or trust deriving the value of its property directly or indirectly principally from real property located in Japan, and (3) where the real property is located in the United States, a "United States real property interest" within the meaning of section 897(c) of the Code. This amendment brings the provision in line with the Foreign Investment in Real Property Act.

Relief from Double Taxation

Article 23 of the US-Japan DTT, which establishes mechanisms for providing relief from double taxation, is amended by the Japan Protocol to align with changes in Japanese law. Under the amended provision, as under the current US-Japan DTT, Japan agrees to allow its residents, subject to relevant domestic laws, a credit against Japanese tax for US taxes paid in accordance with the provisions of the US-Japan DTT. The amended article includes a re-sourcing rule that ensures that Japanese residents can obtain a Japanese foreign tax credit for US taxes paid when the US-Japan DTT assigns the United States primary taxing rights. Under the new provision, Japan also agrees to exclude from the basis of Japanese taxes any dividends paid by a US-resident company to a Japanese-resident company, effectively cementing into place a participation exemption for most US source dividends.

Arbitration

The Japan Protocol amends the mutual agreement article of the US-Japan DTT to include mandatory, binding arbitration to resolve cases before the competent authorities of the United States and Japan. In general, if the competent authorities have not resolved the case within two years, a taxpayer may request that the case to be resolved through arbitration. Arbitration is not available with respect to certain cases. If a court or administrative tribunal in either the United States or Japan has rendered a decision with respect to the case, or if the competent authorities of both the United States and Japan have agreed that the case is not suitable for arbitration, the case cannot proceed to arbitration. In addition, only cases arising from instances of double taxation provided for in the US-Japan DTT are eligible for arbitration. This means that cases brought pursuant to the discretionary authority in paragraph 3 of Article 25 for the competent authorities to consult for the elimination of double taxation "in cases not provided for" in the US-Japan DTT are not eligible for arbitration.

Exchange of Information

The Japan Protocol includes an updated exchange of information article. The new provision allows for the exchange of information which is "foreseeably relevant" for carrying out the US-Japan DTT or domestic law. This phrase is meant to be consistent with section 7602 of the Code, and it conforms with a 2005 change to the OECD Model Tax Convention, which changed the language from "necessary" to "foreseeably relevant". While this provision is intended to provide for the exchange of information "to the widest extent possible", the Japan Technical Explanation notes that neither the United States nor Japan is permitted to use the provision for "fishing expeditions".

The exchange of information provision prevents the United States and Japan from obtaining and exchanging information in violation of local law, and in particular, information protected by attorney-client privilege. Information held by banks, other financial institutions, nominees, or persons acting in an agency or fiduciary capacity is not granted the same protection. This provision effectively overrides domestic bank secrecy laws. The provision also requires the disclosure of beneficial owners of shares or other ownership interests.

This new exchange of information provision has effect from the date of entry into force of the Japan Protocol, without regard to the taxable year to which the matter relates.

Mutual Assistance

The Japan Protocol adds an updated Article 27, pursuant to which the United States and Japan agree to make reasonable efforts to lend assistance in the collection of "revenue claims" on behalf of the other Contracting State. This includes taxes, interest, costs of collection, additions to such taxes, and civil or administrative penalties. Because this provision is not limited by Article 1 or Article 2 of the US-Japan DTT, this agreement can apply to requests with regard to persons who are not residents of either the United States or Japan, and it can apply to the collection of taxes other than income taxes. This expands the existing mutual assistance provision, which was limited to such assistance as was necessary to ensure that treaty benefits were enjoyed only by persons entitled to those benefits under the treaty. This provision means that Japan becomes one of only a handful of US treaty partners with whom such extensive collection assistance will be allowed. The provision will not become operative until Japan and the United States agree upon its mode of application.

With respect to companies, the mutual assistance provision only applies to revenue claims that (1) are not eligible for the mutual agreement procedure; (2) have been resolved through the mutual agreement procedure; or (3) are with respect to a case for which the company has terminated the mutual agreement procedure.

Effective Date

The Japan Protocol enters into force upon the exchange of instruments of ratification, and it goes into effect with respect to taxes withheld at source, such as those taxes on dividends, interest, and royalties, for amounts paid or credited on or after the first day of the third month following the date on which the Japan Protocol enters into force. For all other taxes, the Japan Protocol goes into effect for any taxable period beginning on or after January 1 of the year following the Japan Protocol's entry into force. The various administrative provisions (e.g., relating to mandatory binding arbitration, exchange of information, and assistance in collection) go into effect upon the Japan Protocol's entry into force, without regard to the taxable years involved.

Luxembourg

The Protocol (the "Luxembourg Protocol") Amending the Convention between the Government of the United States of America and the Government of the Grand Duchy of Luxembourg for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (the "US-Luxembourg DTT") was signed on May 20, 2010. The Luxembourg Protocol modernizes the existing US-Luxembourg DTT, which dates from 1996, by bringing the exchange of tax information provisions into conformity with current US and Luxembourg domestic tax policy.

Exchange of Information

Article 28 of the US-Luxembourg DTT concerning the Exchange of Information has been updated with new rules on the exchange of information. Article 28 sets out the obligation to obtain and provide information to the other Contracting State that is foreseeably relevant for carrying out the provisions of the US-Luxembourg DTT or the laws of either state concerning domestic taxes of every kind applied at the national level. The taxes covered by Article 28 include (in addition to income taxes) the US estate, gift, and excise taxes, and with respect to Luxembourg, value added taxes. The Luxembourg Protocol enables the United States and Luxembourg to obtain information from the other State (including financial institutions) without regards to whether the other State would need the information for its own tax purposes. The amended Article 28 concerning Exchange of Information also enables the United States and Luxembourg to obtain such information even if it was protected by the other State's bank secrecy law. The information to be exchanged also includes information relating to the ownership of certain entities. The information subject to the exchange is not limited to information concerning residents of one of the States.

Once the Luxembourg Protocol is in force, the competent authorities of the United States and Luxembourg may seek information under the US-Luxembourg DTT, with respect to a year beginning on or after January 1, 2009.

Spain

The Protocol (the "Spain Protocol") Amending the 1990 Convention between the United States of America and the Kingdom of Spain for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income (the "US-Spain DTT") was signed on January 14, 2013. The Spain Protocol's key modifications to the US-Spain DTT include reducing withholding taxes on dividends, interest, and royalty payments; taxing qualified capital gains in the country of residence of the seller only; modifying the Limitation On Benefits clause; and adding arbitration to the Mutual Agreement Procedure.

Permanent Establishment ("PE")

The time threshold for a PE to be derived from building sites or construction or installation projects is extended from more than six to more than 12 months.

Dividends

The Spain Protocol reduces or eliminates withholding taxes on dividend payments under the following scenarios:

1. the general tax rate for dividends received by a resident of the other Contracting State entitled to treaty benefits is 15%;
2. a reduced tax rate of 5% (currently 10%) applies for qualifying subsidiaries holding a minimum stake of 10% (currently 25%). The reduced tax rate is not applicable to dividend distributions paid by either a Spanish REIT (SOCIMI) or a Spanish Collective Investment Institution;
3. a 0% tax rate if there is a stake of 80% or more held by a corporate shareholder, a twelve months holding period is satisfied, and there is qualification under certain clauses of the revised Limitation On Benefits article; and
4. a 0% tax rate on dividend payments to pension funds.

It is also notable that the Spain Protocol excludes as dividend payments liquidation proceeds.

Interest

As general rule, the Spain Protocol provides that interest paid to a resident of the other Contracting State will be exclusively taxable in the country of residence of the lender (as opposed to allowing a 10% withholding tax under the existing provision). The Spain Protocol contains a few exceptions including certain US source contingent interest payments that do not qualify as portfolio interest under the Code.

Royalties

Royalty payments also follow a residence rule, hence no withholding tax will applicable if the recipient is the beneficial owner (as opposed to the current withholding tax rate of 5%, 8%, and 10% depending on the IP right exploited).

Capital gains

Under the Spain Protocol, capital gains from the alienation of shares that "directly or indirectly entitle the owner of such shares or rights to the enjoyment of immovable property situated in a Contracting State" may be taxed in that

Contracting State. This is a significant change from the existing US-Spain DTT, which allowed a Contracting State (i.e., Spain) to tax a resident of the other Contracting State on the disposition of shares in a company resident in that first State if it owned a substantial participation of at least 25% in the preceding 12 months. Neither the Spain Protocol nor its Technical Explanation explains how the new provision interacts with the existing provision in the US-Spain DTT, which provides that gains from the alienation of stock in a company the property of which consists, directly or indirectly, mainly of real property situated in Spain, may be taxed in Spain (emphasis added). It is also not clear what it means for shares to entitle a shareholder "to the enjoyment of immovable property" in a State (e.g., whether that term suggests some physical use of the property by the shareholder, or whether it is broad enough to encompass a right to dividends paid out of corporate profits that may be derived in whole or in part from the corporation's exploitation of the property).

Branch tax

In line with the tax treatment of dividend payments, under the Spain Protocol, no withholding tax is imposed on the actual or deemed remittance of profits from a PE to its head office if the entity qualifies under certain clauses of the revised Limitation On Benefits clause (otherwise, a 5% branch profits tax rate applies as opposed to 10% currently).

Transparent entities

The Spain Protocol provides that income derived through an entity considered fiscally transparent by either Contracting State shall be considered derived by a resident of one of the Contracting States (the "residence State") under the US-Spain DTT if certain requirements are met: (1) the transparent entity is formed or organized in the US, Spain, or in a third country that has an agreement in force with Spain or the United States (whichever State is the source of the income) containing a provision for the exchange of information on tax matters; and (2) the income is considered to be derived by a resident of the residence State for purposes of the taxation law of that State. This provisions appears designed to modernize language of the exiting US-Spain DTT which had referred to income derived by a "a partnership, estate, or trust" and which had been the subject of a 2006 US-Spain Competent Authority Agreement addressing limited liability companies (LLCs). It also brings the US-Spain DTT more fully in line with the conclusions of the OECD's BEPS Project regarding the application of treaties to hybrid entities.

Limitation On Benefits clause

The Spain Protocol, in line with other US DTTs, contains an updated comprehensive and complex limitation of benefits clause, which seeks to ensure that only certain tax residents in the United States or Spain that have a sufficient nexus with their State can benefit from the DTT provisions. Specifically, a resident company must qualify under one of the following tests: (1) the publicly traded companies test (which allows for trading on not only the US or Spanish stock markets, as under the current US-Spain DTT but also on stock markets in Stuttgart, Hamburg, Düsseldorf, Frankfurt, Berlin, Hannover, Munich, London, Amsterdam, Milano, Budapest, Lisbon, Toronto, Mexico City and Buenos Aires; (2) the subsidiary of a publicly traded company test; (3) the ownership-base erosion test; (4) the active trade or business test; (5) the derivative benefits test; (6) the headquarters company test; or (7) a competent authority determination. The new provision also restricts benefits allowable to income derived through a third State PE of a resident of a Contracting State where if that income is subject to an aggregate effective rate of tax in the residence State and the third State that is less than 60% of the general rate of corporate tax applicable in the residence State.

Mutual Agreement Procedure

Although some limitations may apply, the Spain Protocol includes a mandatory and binding arbitration process if, after two years, the competent authorities have not been able to solve a dispute under the mutual agreement procedure. The Spain Protocol includes a so-called "last-best offer" (or "baseball arbitration") clause under which each country would submit a proposed resolution and the arbitration panel would be required to decide the case by adopting one or the other proposed resolution. This approach, which is consistently used by the United States in its treaty arbitration provisions, tends to discourage countries from taking extremely aggressive positions and thereby tends to promote compromises that resolve disputes. The new provisions will be applicable exclusively to cases submitted to the mutual agreement procedure once the Spain Protocol enters into force.

Exchange of information / Assistance in Collection

A new regime for the exchange of information and administrative assistance has been included in the Spain Protocol by expanding, for example, the scope of information requests to cover taxes not otherwise subject to the provisions of the US-Spain DTT, by introducing the "foreseeably relevant" standard in place of the "necessary" standard, and by ensuring that bank secrecy and "domestic interest" limitations do not restrict the exchange of information. The Spain Protocol also introduces limited authority for one Contracting State to collect taxes on behalf of the other Contracting State (i.e., only to ensure that benefits of the US-Spain DTT are not enjoyed by persons not entitled to those benefits).

Puerto Rico

A Memorandum of Understanding has been signed to initiate negotiations to prevent double taxation on Puerto Rican - Spanish investments.

Effective Dates

The new provisions of the Spain Protocol will be effective as follows: (i) for taxes withheld at source (such as dividends, interest and royalties), the provisions will take effect for amounts paid or credited on or after the date the Spain Protocol enters into force; (ii) for taxes determined with reference to a taxable period, the Spain Protocol will be applicable for taxable periods beginning or on after its entry into force; and (iii) the remaining provisions will be effective from the date the Spain Protocol enters into force.

Switzerland

With the recent US Senate vote to approve ratification of the 2009 Protocol (the "Switzerland Protocol") to the 1996 Convention between the United States of America and the Swiss Confederation for the Avoidance of Double Taxation with Respect to Taxes on Income (the "US-Switzerland DTT"), several key provisions of the US-Switzerland DTT have been changed, including the standard by which information is exchanged thereunder.

Update to Tax Information Exchange

Long a sticking point for US government authorities attempting to enforce US federal tax laws, the tax information exchange provisions of the US-Switzerland DTT will be updated by the Switzerland Protocol to a more modern standard than the "fraud or the like" standard found in the US-Switzerland DTT.

Specifically, the Switzerland Protocol replaces Article 26 of the US-Switzerland DTT in its entirety and authorizes the exchange of information between the United States and Switzerland where such information "may be relevant" to carrying out the US-Switzerland DTT or the administration or enforcement of domestic tax laws so long as the taxation is not contrary to the treaty. Notably, the information subject to the exchange is not limited to information concerning residents of one of the countries. Consistent with modern standards, the new provision also ensures that bank secrecy and "domestic interest" limitations do not restrict the exchange of information.

The new tax information exchange provisions apply to any information that relates to a date on or after the signing of the Switzerland Protocol and to any tax year after 2009.

Exemption for Dividends Paid to Pension Fund

The Switzerland Protocol modifies the Dividends article to expand the exemption from taxation for dividends paid by corporations in one country to pension or other retirement arrangements resident in the other country to include individual retirement savings plans established and owned by a resident of the other country, provided that the competent authorities agree that the individual retirement savings plan established in the other State corresponds to an individual retirement savings plan recognized for tax purposes in the source State.

Mandatory Competent Authority Arbitration

The Switzerland Protocol also institutes mandatory (rather than optional) binding arbitration between the United States and Swiss competent authorities under the mutual agreement procedure of Article 25 of the US-Switzerland DTT if a mutual agreement cannot be reached within two years of the commencement of a MAP case. As in the case of the other US tax treaty arbitration provisions, the Switzerland Protocol's provision calls for "last best offer" arbitration. The new arbitration requirement applies to cases that were under MAP consideration when the Switzerland Protocol enters into force, as well as to subsequently initiated MAP cases.

Impact on Taxpayers

United States

United States taxpayers, including US and other multinational corporations, have a significant interest in a number of specific issues addressed by the Protocols. However, the larger impact of the ratification of the Protocols may simply be that they have, in fact, been ratified. The earliest of these four Protocols had languished in the US Senate for more than nine years and the latest of these four Protocols had languished in the US Senate for more than six years.

United States Senator Rand Paul (R-KY) has been the primary impediment in the Senate, blocking ratification for years based on privacy concerns, according to US Senate Majority Leader Mitch McConnell (R-KY). There has been no clear path for any income tax treaty or protocol to be ratified in the Senate and the US Treasury Department ("Treasury") has not, unsurprisingly, signed a treaty or protocol since 2013. The ratification of these four Protocols would appear to alleviate this blockage. The US Senate had hoped attempt to take up three pending treaties with Chile, Hungary, and Poland next. However, the latter three treaties may first need to be re-negotiated after Treasury flagged issues that may need to be revised in light of US tax reform. The ratification of the Protocols and treaties will also hopefully encourage Treasury to secure additional agreements (e.g., with South American countries) in the near future.

Beyond the information exchange provisions which so concerned Senator Paul, the Protocols resolve a number of issues that will have a positive impact on many US taxpayers. As noted above, for example, both the Spain Protocol and the Japan Protocol eliminate withholding taxes on interest (as well as royalties in the case of the Spain Protocol). In addition, the Japan Protocol, the Spain Protocol, and the Switzerland Protocol each provide for mandatory binding arbitration of certain cases where the competent authorities have not been able to reach agreement.

Japan

The Japan Protocol puts into place three major procedural changes to the underlying US-Japan DTT: arbitration, expanded exchange of information, and mutual assistance.

The addition of mandatory, binding arbitration provides a significant incentive for the competent authorities to resolve cases in a timely manner. Taxpayers should look out for further developments with respect to arbitration between the United States and Japan. The exact procedures for requesting and conducting arbitration will be established by separate agreement. In addition, pursuant to the resolution of advice and consent to ratification passed by the Senate, once ten arbitrations have been completed under any US treaty that includes arbitration, the Secretary of the Treasury must provide the Senate with a report detailing the operation and application of the arbitration mechanism. This report could provide information taxpayers may use to assess the viability and effectiveness of arbitration. Based on the growing number of US treaties that now include arbitration, this threshold may soon be met.

The two other procedural changes should be closely monitored by relevant taxpayers. Both the expansion of the exchange of information and the provision of mutual assistance in collection of taxes demonstrate increased cooperation between the United States and Japan with respect to enforcement.

The Japan Protocol also favorably expands the withholding exemption with respect to dividends. Under the new language, 50-50 owners should be eligible for the exemption. In addition, the source-country exemption with respect to interest should also favorably expand treaty benefits.

Luxembourg

The Luxembourg Protocol broadens the exchange of information provisions of the US-Luxembourg DTT. Following the ratification of the Protocol, the amended Article 28 permits the IRS to make requests on an expanded basis. When information is requested by a Contracting State in accordance with Article 28, the other Contracting State is obligated to obtain requested information even if that State has no direct tax interest in the case. A Contracting State is obligated to provide such information even if such information is held by financial institutions, nominees, or persons acting in an agency or fiduciary capacity. Because Article 28 supersedes any applicable bank secrecy laws, this article also requires the disclosure of information regarding the beneficial owner of an interest in a person such as the identity of a beneficial owner of bearer shares. Under the expanded Exchange of Information provisions, the competent authorities of the United States and Luxembourg have the authority to obtain and exchange upon request information held by financial institutions, nominees, or persons acting in an agency or fiduciary capacity, including nominees and trustees.

Spain

The Spain Protocol does the most of any of the newly passed protocols to amend and modernize a pre-existing DTT. The Spain Protocol will reduce the tax rates levied on various types of qualifying income, including dividends, interest, royalties, and some capital gains. The Spain Protocol will put Spain on a more equal footing with other countries that have already modernized tax treaties with the United States. It is thus expected that the Spain Protocol will facilitate cross-border investments between the United States and Spain due to this impact on the taxation of cross-border income flows between the two countries.

The 0% tax rate on parent-subsidiary dividends should have a positive impact on US corporate entities investing in Spain via fully owned or controlled Spanish subsidiaries and for US entities planning the creation of an EU-wide holding entity in Spain. Additionally, the taxation on interest payments under the country of residence of the lender rule will harmonize cross-border financing between the US group companies and financial institutions with their EU counterparts to the extent interest payments made from Spain to EU lenders are generally tax exempt.

For US taxpayers seeking to transfer their IP to Spain, the new rules regarding an exemption on royalty payments may decrease the litigation risk for US group companies. Before the passing of the Spain Protocol, the Spanish tax authorities approach in this area was quite litigious.

One should also note that, with updated Exchange of Information, Mutual Agreement Procedure, and Limitation on Benefits provisions, relations between the tax authorities in Spain and the United States have also been modernized, reflecting bilateral efforts to crack down on tax evasion. Taxpayers that rely on the US-Spanish DTT for their tax planning may generally face greater scrutiny under the new rules now that the investigation powers of the tax authorities of both countries have been strengthened, and taxpayers may wish to review their eligibility for treaty benefits under the updated Limitation on Benefits provision.

Switzerland

The major change of the Switzerland Protocol is the update to the tax information exchange provisions. Under the US-Switzerland DTT, the IRS is required to meet a "fraud or the like" standard when submitting requests for information. Mere noncompliance, however egregious, was not sufficient if no fraud was involved.

The new Article 26 in the Switzerland Protocol paves the way for IRS requests on an expanded basis, including pursuant to the FATCA intergovernmental agreement between Switzerland and the United States. Under the FATCA intergovernmental agreement, the United States may make group requests for information related to US accounts where the account holder did not consent to FATCA reporting by a Swiss financial institution and for information related to certain payments made to nonparticipating foreign financial institutions.

Currently, the IRS receives aggregated and pooled information each year from Swiss financial institutions on the number and aggregate value of all nonconsenting US accounts that they maintain, as well as aggregate information on certain reportable payments made to nonparticipating foreign financial institutions during the year. With the Switzerland Protocol, the IRS will be able to request specific and unredacted information related to these account holders and financial institutions, as contemplated by the intergovernmental agreement. Given the short deadline of 10 days for producing the requested information under the intergovernmental agreement, Swiss financial institutions may consider preparing data and information on their pools of nonconsenting US accounts and on payments made to nonparticipating foreign financial institutions.

Outside of FATCA, over 80 Swiss banks have signed non-prosecution or deferred prosecution agreements with the US Department of Justice pursuant to which many provided detailed but often redacted information on accounts held directly or indirectly by US taxpayers. With the Switzerland Protocol's entry into force, the IRS will now have the means to obtain detailed information on these US taxpayers.

For investments made through Swiss Pillar 3 retirement plans and US Individual Retirement Accounts, the Switzerland Protocol should eliminate the dividend withholding tax rate on dividends paid by non-controlled corporations resident in the other country. Currently, there would be a 15% withholding tax under the US-Switzerland DTT.

Conclusion

Although it has taken nearly a decade, the newly updated DTTs with Japan, Luxembourg, Spain, and Switzerland indicate the United States' ongoing commitment to modernizing its network of international tax treaties. The changes these protocols will bring are expected to encourage more bilateral investments while generally bolstering the US government's efforts to identify and investigate taxpayers believed to be evading US federal taxes.

Under the amended treaties, treaty partners Spain, Japan, Luxembourg, and Switzerland will also be able to avail themselves of the updated provisions to investigate taxpayers that are based in the United States, or have financial accounts in the United States. Meanwhile, treaties with Poland, Hungary, and Chile, which have also pending for nearly a decade, are still on hold. The Senate Foreign Relations Committee has deferred its consideration of these three treaties because ranking member Senator Menendez raised concerns regarding the US Department of the Treasury's reservations that address the Base Erosion and Anti-Abuse Tax provisions of the 2017 US tax reform legislation, the Tax Cuts and Jobs Act. Treasury and Senate Foreign Relations are working together to find a resolution that would permit these three treaties to move forward. There is currently no word on whether and when the Senate Foreign Relations Committee will consider the Protocol amending the Convention on Mutual Administrative Assistance in Tax Matters, which was agreed to on May 27, 2010 and first submitted to the Senate on May 17, 2012.

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