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Provisions of current US tax bill include withholding requirements

The current 2025 tax Bill as recently passed by the US House of Representatives includes a new US Internal Revenue Code Section that could significantly impact the income streams of portfolio investors.

Background

The United States has an existing defensive tax on nonresidents which was enacted in 1934, though it has to date been unused. 26 USC Section 891 "Doubling of rates of tax on residents of certain foreign countries", states that *"Upon a determination by the President that, under the laws of any foreign country, citizens or corporations of the United States are being subjected to discriminatory or extraterritorial taxes, and upon his proclamation to this effect, rates of taxes imposed...." "...shall be doubled in the case of each citizen and corporation of such foreign country..."*

Observations:

– Section 891 applies broadly to income earned by non-US citizens.

– There has been no known contemporary use of this Section (lies dormant absent "determination by the President" trigger).

– Tax types covered by this Section are expansive, and include income, gains from the sale of US real property, and other items of income BBH ordinarily pay to our non-US resident client base, however, as Section 891 does not address corresponding withholding responsibility, any additional liability presumably would be self-assessed.

Current proposal: Timeline and legislative developments

On May 22, 2025, the House of Representatives passed the One Big Beautiful Bill Act ("OBBBA"). The OBBBA incorporates certain parts of the "Defending American Jobs and Investment Act" (H.R. 591) and the "Unfair Tax Prevention Act" (H.R. 2423) proposed earlier this year.

– OBBA creates a new US Income tax Code Section (899) which could impose and increase statutory US nonresident tax rates in 5-percentage point annual increments up to a maximum of 20 percentage points above the statutory rate.

– Also included is a requirement of the US Treasury Department to submit a report listing each foreign country that has been determined to have one or more extraterritorial or discriminatory taxes which are defined as "unfair" to US citizens.

– The effect of country's appearance on a "list" was to impose an additional 5% penalty tax on the applicable US nonresident tax rates (e.g., NRA, FIRPTA, ECI) to residents and companies of the listed countries. This penalty tax would apply from January 1st of the year following the country's appearance on the list, increase by 5% annually until the country was removed from the list.

– Importantly, the proposal invokes US nonresident withholding responsibility on withholding agents making payments that would be subject to the additional tax.

This provision was included in the first House draft of "One Big Beautiful Bill", and at this date remains as a revenue-raising provision with incremental modifications from the HR 591 proposal in the version that now sits with the US Senate for consideration.

Status as of publication date

Introduced	Passed House	Passed Senate	To President	Becomes Law	Effected (Treasury regulations finalized)

"Discriminatory Tax" as presently defined

A "discriminatory tax" is defined as meeting one of four definitions:

1. The tax applies to items of income that would not be from sources within the foreign country under US income tax rules if the sourcing rule were applied by treating the foreign country as though it was the US.
2. The tax is imposed on a base other than net income and does not allow a recovery of costs and expenses.
3. The tax is exclusively or predominantly applicable in practice or by its terms to nonresident individuals or foreign corporations or partnerships by treating the foreign country as though it were the US due to specified factors or restrictions, and similarly situated foreign corporations and partnerships that supply comparable goods and services which are excluded from the tax.
4. The tax is not treated as an income tax under the laws of the foreign country or is viewed as outside the scope of a double tax treaty.

Considerations:

– Under the current bill, the definition of "discriminatory tax" does not include 1) withholding taxes, 2) value-added tax (VAT), 3) goods and services tax, 4) sales tax or similar (tax on consumption), 5) taxes imposed on a per-unit or per-transaction basis rather than on an ad valorem basis, 6) taxes on real or personal property, and 7) "any other similar tax identified by the Treasury Secretary as not discriminatory".

– There are noted considerations of the view that certain digital services taxes, royalty re-sourcing rules, diverted profits taxes, taxes on intellectual property, as well as aspects of the Organisation for Economic Co-operation and Development (OECD) Pillar II regime provisions are viewed by the US as discriminatory.

Potential impact to portfolio investors

Residents of countries that presently have what could meet the definition of "Discriminatory Taxes" outlined above could be subjected to an additional and gradually increasing 5% withholding tax on US source income including certain interest, dividends, income that is effectively connected with a US trade or business, or that is not exempted from the scope of the proposal.

Such provisions could over time prove to have an increasingly material impact on US portfolio investment income yields.

Potential impact to financial intermediaries and US withholding agents

If passed, Financial Institutions (including entities acting as Qualified Intermediaries, non-Qualified Intermediaries, and Withholding Agents) would need to adapt US nonresident tax withholding systems and reporting models, encompassing:

1. Withholding capabilities

– Technology and capabilities required to apply more than one statutory rate by income type.

– Technology and capabilities required to apply higher statutory rates by jurisdiction and treaty status.

2. Reporting capabilities

– Systems development required to apply any new reporting codes required under additional reporting rules.

3. Change monitoring, communication, and tax rate implementation/change

– Design and implement research "list monitoring" and operational periodic and annual "rate/profile update" processes.

4. Modification of withholding delegation instructions (Withholding agents and intermediaries that use pooled accounts)

– Intermediaries may need to alter withholding instruction mechanisms and/or establish additional pool accounts at higher rates (and transfer of applicable assets).

5. Development and implementation of requirements outlined in corresponding treasury regulations

Conclusion

Brown Brothers Harriman (BBH) has been monitoring these proposals and developments and has a longstanding history of working with our clients to assist in the implementation of support models enabling compliance with US tax regulatory changes. BBH will continue to monitor and communicate updates as these proposals move through the legislative and regulatory development process.

If you would like to learn more about these operational challenges and opportunities, please contact:

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