

TAX TREATY TREATMENT OF TAX CREDITS WHEN MOVING FROM A  
CREDIT TO AN EXEMPTION SYSTEM  
FOR MSSRS. THOMAS & EDGE

Submitted by Chairman Dave Camp

**And answered by Stephen Edge in bold below**

Concerns have been raised about the status of the United States' tax treaty network if the United States moves from an international tax system that allows a tax credit to be taken for foreign income taxes paid, to a system that exempts certain dividends paid by foreign subsidiaries from taxation. As with many countries that tax worldwide income, U.S. tax treaties generally state that the U.S. will provide a credit against foreign income taxes. The Committee, however, is considering whether the U.S. should move to a system that provides an exemption for certain dividends paid by foreign subsidiaries, in lieu of a foreign tax credit. How did your country deal with its tax treaties when moving from a credit to an exemption system? Was this discussed, or will your tax treaties need to be renegotiated?

**The UK has not had to change its double tax treaties. The reason for this is that most of the UK's treaties are like that between the United Kingdom and the USA and so provide that credit for foreign taxes is only to be allowed within any constraints provided therefor in United Kingdom law and also that credit is required to be given only against UK taxes on the same income. Where a dividend from overseas does not qualify for exemption under our new territorial regime (possibly because of the application of certain anti-avoidance rules), these rules will continue to operate and credit will be given in accordance with domestic law against UK tax on the same income. Where, however, the foreign dividend is exempt, then there will be no foreign tax credit claim to be made because of the absence of UK tax on the same income and there will also be no spill-over of unused foreign tax credits against UK tax due on other income because of the "same income" limitation. In most cases, therefore, the treaty credit provisions will simply have become irrelevant and will thus be redundant.**