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Treasury Department Asks Congress to Drop Proposed Legislation to Increase Tax Rates on Non-US Investors From Certain Countries

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On May 22, the US House of Representatives passed the "One Big Beautiful Bill Act" (OBBBA). Among other things, the House bill proposed to add Section 899 to the Internal Revenue Code, which would have increased US tax rates on individuals and business entities resident in – and governments of – "discriminatory foreign countries." The proposal, termed a "revenge tax," was largely in response to the "Pillar Two" global minimum tax framework of the Organisation for Economic Co-operation and Development (OECD).

Cooley has previously discussed tax proposals in the House bill, including the limitation on the deductibility of state and local taxes in **this June 2 client alert**, as well as the temporary suspension of the amortization requirement for domestic research and experimentation expenditures in **this June 4 client alert**.

House bill

The House bill took aim at "discriminatory foreign countries" that impose "unfair foreign taxes" on US persons. For purposes of Section 899, "unfair foreign taxes" would have included any foreign tax imposed under an undertaxed profits rule (UTPR), digital services tax (DST) and diverted profits tax (DPT), but would have excluded any tax that does not apply to any US person or to any "controlled foreign corporation" (CFC) that is more than 50% owned by US persons. The Department of the Treasury also would be able to designate other "extraterritorial" or "discriminatory taxes" as unfair foreign taxes, including any tax enacted "with a public or stated purpose indicating the tax will be economically borne, directly or indirectly, disproportionately by United States persons" compared to persons resident in the taxing jurisdiction.

The House bill would have increased certain US tax rates that apply to applicable persons from a discriminatory foreign country. In general, the US tax rate would have increased by 5% for each year, capped at 20% above the statutory rate (determined without regard to any rate applicable in lieu of such statutory rate). In instances where these taxes are imposed by means of source-based withholding by US payors, the withholding rates would have been increased accordingly. The increased tax rates would have applied to individuals and business entities that are resident in or have other connections to discriminatory foreign countries, and to US payors obligated to withhold on payments to such persons. For purposes of Section 899, "applicable persons" would have included governments of discriminatory foreign countries, as well as certain resident individuals, corporations, private foundations, nonpublic foreign corporations, trusts, partnerships, branches and other entities identified with respect to such countries by Treasury.

The House bill also would have disallowed the favorable tax treatment afforded to foreign governments and certain related entities, such as sovereign wealth funds, of discriminatory foreign countries.

On June 16, the US Senate Finance Committee passed a version of the OBBBA, which retained Section 899.

Treasury announcement/Senate bill

On June 26, Treasury announced an agreement with other G-7 countries. Under this agreement, according to a social media post by Treasury Secretary Scott Bessent, the OECD Pillar Two taxes will not apply to US companies. In return, Treasury requested that Section 899 be removed from the OBBBA.

On June 28, the Senate released its version of the OBBBA, which did not include Section 899. On the same day, the G-7 announced an agreement to pursue a "side-by-side" system that would exclude US-parented groups from some aspects of Pillar Two.

Next steps

With the Senate having passed its version of the OBBBA, House and Senate negotiators will now work to prepare a final bill. Although the final form of the bill is not yet known, we would expect that Section 899 will not be included. Cooley will continue to monitor as the US legislative process unfolds.

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