# BUDGET RESOLUTION TAX PROVISIONS CONTAIN REPRISAL TAX AIMED AT O.E.C.D. PROPOSALS

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## INTRODUCTION

On Friday, May 22, 2025, the U.S. House of Representatives adopted a budget resolution containing provisions that would impose increased taxes for persons based in countries that impose taxes found to discriminate against U.S. companies or their subsidiaries.[1] In broad terms, if a country is determined to have "crossed the line," residents of that country and their subsidiaries would face up to a 20% increase in withholding taxes on U.S. source investment income, income taxes on income that is effectively connected to the conduct of a U.S. trade or business, and certain other taxes. The tax increase will be effected in 5-percentage point increments over a 4-year period, ultimately resulting in a 20-point increase in tax beginning in 2026.

### Targets

The provision is intended to have broad application, covering the following persons and entities:

- Foreign governments, sovereign wealth funds, and public agencies of countries designated as discriminatory foreign countries
- Individuals and legal entities (including corporations, partnerships, trusts, and foundations) that are resident in, established in, or effectively managed in a discriminatory foreign country
- Entities that are substantially owned or controlled, directly or indirectly, by any of the above persons after application of broad ownership-by-attributions rules

Tax regimes that are expressly considered to be discriminatory include the following:

- Taxes that implement the Undertaxed Profits Rule of the O.E.C.D. These taxes are designed so ensure a global minimum tax of 15%, which is primarily enforced by an income inclusion rule at the parent level of a group and secondarily enforced by an income inclusion rule or a deduction disallowance rule wherever the multinational group operates.
- Digital Services Taxes on revenues earned by large multinational digital companies. These taxes are imposed on activities such as online advertising, operation of digital marketplaces, and user data sales. They target companies that generate significant revenue from users in a country without having a physical presence in that country.

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[1] Proposed Code §899 (Enforcement of Remedies Against Unfair Foreign Taxes.)

 

- Diverted Profits Taxes designed to counteract aggressive tax planning within multinational groups. From the viewpoint of the country in which the customer is based, the tax targets arrangements that divert profits to a low-tax jurisdiction, often through complex structures or transactions lacking genuine economic substance.

- Any other extraterritorial tax, discriminatory tax, or other tax enacted with a public or stated purpose that the tax be economically borne, directly or indirectly, disproportionately by US persons as determined by the Secretary of the Treasury.

**Implementation Schedule**

In general, the implementation date for imposing the tax increase against a particular foreign jurisdiction is the first day of the calendar year following the year in which the latest of the following events occurs:

- 90 days after the enactment, which generally targets persons in jurisdictions that have already adopted a targeted foreign tax

- 180 days after the enactment of an unfair foreign tax, which generally targets persons in jurisdictions that adopt a discriminatory foreign tax after the 90-day period mentioned above

- The initial effective date of the unfair foreign tax, which generally targets persons in jurisdictions that adopt a targeted foreign tax

Withholding agents will not be penalized for under-withholding regarding amounts paid prior to 2027, subject to a good faith requirement.

**Increased Taxes**

In addition to income taxes and withholding taxes on investment income, several other taxes will be increased if the measure is adopted in present form. They include

- Code 59A (Tax on Base Erosion Payments of Taxpayers With Substantial Gross Receipts),

- Code §884 (Branch Profits Tax),

- Code §897 (Disposition of Investment in United States Real Property),

- Code §1441 (Withholding of Tax on Nonresident Aliens),

- Code §1442 (Withholding of Tax on Foreign Corporations),

- Code §1443 (Foreign Tax-Exempt Organizations),

- Code §1445 (Withholding of Tax on Dispositions of United States Real Property Interests),

- Code §1446 (Withholding of Tax on Foreign Partners' Share of Effectively Connected Income), and

- Code §4948 (Application of Taxes and Denial of Exemption With Respect to Certain Foreign Organizations).

## PATH FORWARD

The measure awaits consideration by the Senate. As in the House of Representatives, the Republican Party is the majority party in the Senate. Assuming the measure is adopted more or less in present form, the O.E.C.D. and the E.U. face a Hobson's Choice. The above taxes could be repealed, without substitute measures that might run afoul of Code §899. In that scenario, the effect of Code §899 will be minimal, just as the effect of another reprisal tax provision, Code §891,[2] which was enacted in 1934, and has never been invoked by a sitting President, although it was successfully threatened against France at the time of enactment.[3]

On the other hand, if those taxes come into effect, Code §899 will disrupt trade patterns, especially if other defense tactics are adopted by the U.S., the O.E.C.D., and the E.U.

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2 Code § 891 (Doubling of Rates of Tax on Citizens and Corporations of Certain Foreign Countries.) In pertinent part, it provides as follows:

> Whenever the President finds that, under the laws of any foreign country, citizens or corporations of the United States are being subjected to discriminatory or extraterritorial taxes, the President shall so proclaim and the rates of tax imposed by section 1 , 3 , 11 , 801 , 831 , 852 , 871 , and 881 shall, for the taxable year during which such proclamation is made and for each taxable year thereafter, be doubled in the case of each citizen and corporation of such foreign country; but the tax at such doubled rate shall be considered as imposed by such sections as the case may be. In no case shall this section operate to increase the taxes imposed by such sections (computed without regard to this section ) to an amount in excess of 80 percent of the taxable income of the taxpayer (computed without regard to the deductions allowable under section 151 and under part VIII of subchapter B).

3 See Joseph J. Thorndike, "Tax History: Threats, Leverage, and the Early Success of Reprisal Taxes," *Tax Notes* (March 21, 2016) .