

Nonresident Alien Income and Tax Withheld, 1982

By Chris R. Carson*

The United Kingdom surpassed both the Netherlands and the Netherlands Antilles as the foreign country with individuals and organizations receiving the most U.S. source income (\$2.2 billion) during 1982. The increased use of "dual resident corporations" [1], which for tax purposes are considered resident in both the United States and the United Kingdom, is primarily responsible for the sudden rise in interest payments to the United Kingdom. Dual resident corporations can deduct from income in both countries interest payments and certain costs of starting a business.

Although U.S. source income paid to the Netherlands Antilles, a tax haven, rose by 13 percent from 1981 [2], future payments may be less due to the Deficit Reduction Act of 1984. This legislation exempts most new debt issues from U.S. withholding tax, at least partly reducing the withholding tax and interest rate advantages that U.S. corporations derive by borrowing funds through the Netherlands Antilles. Interest, which makes up 93 percent of U.S. source income paid to the Antilles, has been substantially exempt from withholding under an extension of the United States-Netherlands tax treaty.

U.S. source income paid to foreign individuals and organizations rose just over 9 percent, to \$10.6 billion, from 1981 to 1982. For the first time, interest surpassed dividends as the most common type of income, as 48 percent or \$5.1 billion of all income paid represented interest. This reflects the growing use of borrowed foreign capital in helping to finance the U.S. economic recovery. Although dividends rose to \$4.5 billion, their share of all income fell to 43 percent from 45 percent in 1981.

BACKGROUND INFORMATION

A U.S. individual or organization paying income to a nonresident alien (foreign individual, corporation, or other organization) reports this income and the U.S. tax withheld on the Form 1042S. While the basic tax rate is 30 percent, certain types of income are taxed at different rates. Income paid to countries

that have entered into tax treaty agreements with the United States is usually taxed at lower rates. The tax withheld represents final payment of the actual tax liability in almost all instances. Income connected with the recipient's U.S. trade or business is exempt from withholding. The United States taxes this income separately, as though it were received by a U.S. citizen or corporation.

The responsibility for withholding tax belongs to the payor or the representative (usually a financial institution) of the payor rather than the recipient of the income. This is because the United States has no agreements with foreign countries (as they would be impractical) authorizing direct taxation of foreign individuals and organizations that are not resident in this country. Direct taxation of nonresident aliens would be difficult to enforce. The basic tax rate on nonresident alien income (30 percent) differs from the graduated tax rates for U.S. individuals and corporations because foreign individuals and corporations may receive income from an indefinite number of U.S. payors. Since the nonresident alien is not required to file a tax return and consolidate all U.S. income, the total income cannot be taxed in graduated "brackets," as one payor would have no knowledge of the amount of income other U.S. persons had paid to the same nonresident alien.

RECENT LEGISLATION

The Deficit Reduction Act of 1984 exempts certain interest payments from withholding. To qualify, this interest must be paid on debt issued after the establishment of the Act (July 18, 1984). Interest paid to a foreign individual or corporation owning 10 percent or more of the voting shares of the U.S. payor does not qualify for this exemption.

Before the passage of this legislation, some foreign investors were hesitant to invest in the United States because of the 30-percent withholding tax. Often foreign individuals and corporations that would be taxed on this income in their own countries, but could not credit the associated U.S. tax withheld, would choose

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to invest only in their own countries to avoid double taxation. Individuals and organizations that wanted to avoid income taxes in their own countries might also avoid investments subject to withholding.

In the late 1970's, high U.S. interest rates made U.S. investments attractive to foreign individuals and organizations. Large U.S. trade deficits left billions of U.S. dollars in foreign countries available for investment. U.S. multinational corporations, seeing the possibility of borrowing large amounts of money at interest rates below U.S. rates, set up finance subsidiaries in the Netherlands Antilles. These subsidiaries borrowed large amounts of money from the Eurobond market and loaned the money to the U.S. parent corporation. The interest payments from the U.S. parent to its subsidiary were exempt from withholding under an extension of the U.S. tax treaty with the Netherlands. Smaller companies, which needed to borrow less money, were substantially shut out of the Eurobond market as the cost of setting up and maintaining a finance subsidiary in the Netherlands Antilles was prohibitive when compared to their potential interest savings.

The U.S. Treasury Department began to renegotiate the U.S. tax treaty with the Netherlands Antilles. While this treaty was being renegotiated, renewed attention was given to earlier proposals to exempt certain interest from U.S. taxation regardless of what country the interest was paid to. The prospect of U.S. tax exempt interest would spur foreign investment in the United States and in turn create new jobs. The amount of revenue loss was estimated to be relatively small, as only \$152.5 million of tax was withheld on interest income for 1982. The revenue effect of the exemption of this interest income from withholding will not be felt immediately by the Treasury, as debt issues made prior to the Deficit Reduction Act will still be subject to withholding (except when exempted by tax treaties). In addition, any withholding tax revenue loss would be partly offset by a reduction in foreign tax credit for some U.S. corporations now crediting the small amount of tax paid to the Netherlands Antilles on the net interest income (interest income from U.S. parent minus interest paid to bondholder) of the U.S. controlled finance subsidiaries there. As the money would be borrowed directly from the bondholder (usually European), there would be no net interest income subject to Antilles tax. The Deficit Reduction Act of 1984 also recharacterizes certain income of foreign subsidiaries as U.S. income. This will prevent some corporations from earning low-tax foreign income in the Antilles (and elsewhere) to increase their credit limitation and thereby claim a greater foreign tax credit.

As a result of the exemption of certain interest income from withholding tax, small U.S. companies and the U.S. Treasury will now be able to enter the Eurobond market directly. The entrance of smaller U.S. companies and the U.S. Treasury into the Eurobond market may cause increased competition for low-cost foreign debt. This competition is likely to drive up foreign interest rates on this debt closer to the U.S. level. The possibility of this interest rate increase may have been the reason that some U.S. corporations issued hundreds of millions of dollars in Eurobonds recently, in expectation of the passage of the Deficit Reduction Act of 1984. Downward pressure may be put on domestic interest rates, as U.S. lenders will have less demand for new debt from these small companies and the U.S. Treasury. The demand for dollars to invest in the United States should strengthen the dollar, making imports cheaper and exports more expensive. As foreign interest rates approach the U.S. rate, foreign individuals and organizations will shift new investments to their own countries until a point of equalization is reached.

DATA ANALYSIS AND TRENDS

Although income rose faster (9 percent) from 1981 to 1982 than tax withheld (2 percent), both rose slowly compared to their increases for 1981 (45 percent and 18 percent, respectively). Income exempt from withholding increased by 27 percent, while income subject to withholding actually fell by 2 percent. Almost half of this increase in exempt income was accounted for by the United Kingdom, where exempt income increased by over \$470 million. The total increase in exempt income was nearly a billion dollars.

The amount of average income per payment rose by 11 percent to \$18,800 from 1981 to 1982. This contrasts sharply with a 54-percent increase in 1981. Corporate recipients again received much larger average payments (\$144,000) than other recipients, including individuals (\$1,800). The increase in the size of the average payment to corporations, up from \$92,000 in 1981, is due more to the drop in the number of Forms 1042S showing payments to corporations, from 76,036 to 51,962, than in the increase in corporate income (4 percent).

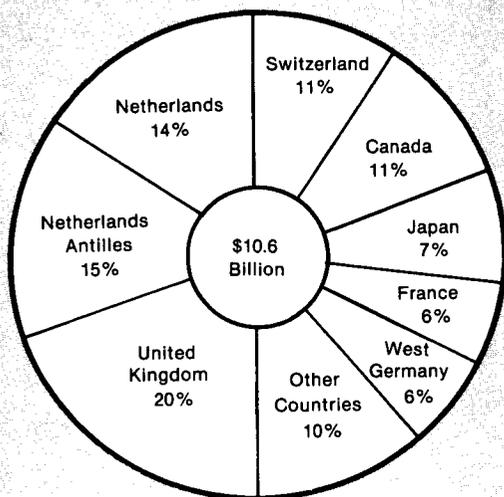
Country of Recipient

The eight countries shown in Figure A accounted for 90 percent of all U.S. source income. These countries accounted for 88 percent of all income in 1981. The United Kingdom dominates this list, receiving a higher portion of the total, 20 percent, than any country has received in recent years.

While these countries' U.S. source income rose 12 percent from 1981, the distribution of this income has changed dramatically. As shown in the following table, income paid to the United Kingdom rose by 60 percent from 1981. Japan and the Netherlands Antilles also received substantially more income than in 1981, posting gains of 35 percent and 13 percent, respectively. The Netherlands, Canada, and Switzerland actually received less U.S. source income than in 1981.

The dramatic increase in income payments to the United Kingdom was mainly, as already mentioned, due to the establishment of "dual resident corporations." These are corporations that take advantage of the varying rules that different countries use for determining the residency of a corporation. This allows corporations having losses, especially in starting a new operation or facility, to deduct these losses on the tax returns filed in both countries. Since U.S. corporate residency is determined by the country of incorporation, the "dual resident corporation" must be incorporated in the United States, usually in Delaware. The United Kingdom determines the country of residence of corporations by the country where management occurs.

Figure A
Percent of Total Income Paid, by Country of Recipient, 1982



This combination of U.S. incorporation and U.K. management is typically beneficial when beginning a new investment in the United Kingdom, such as drilling for oil in the North Sea. Certain costs of starting the project, including interest expense, are then deducted from both U.S. and U.K. income. The startup capital is sometimes borrowed from a U.K. lender because the interest rates in recent years have been lower in Europe and interest payments to U.K. individuals and organizations are exempt from U.S. withholding in most instances. Interest payments by these "dual resident corporations" may explain the increase in interest paid to the United Kingdom of nearly \$500 million from 1981 to 1982.

More tax was withheld from payments to the United Kingdom than to any other country. The \$136 million withheld from this income represents 18 percent of all tax withheld by U.S. withholding agents. Almost 94 percent of this tax on U.K. income was withheld from dividends. More than \$100 million of tax was withheld on payments to each of Switzerland and Canada, representing 16 percent and 15 percent, respectively, of all tax withheld.

Gross Income Paid
[thousands]

Country	1981	1982	Change
	(1)	(2)	(3)
United Kingdom	\$1,357,044	\$2,174,506	60%
Japan	519,568	703,643	35
Netherlands Antilles	1,399,528	1,580,359	13
West Germany	598,054	627,861	5
France	652,496	660,975	1
Switzerland	1,201,878	1,176,462	-2
Netherlands	1,539,633	1,463,583	-5
Canada	1,217,255	1,151,846	-5
Other countries	1,213,531	1,085,074	-11

There were substantial increases in the amount of tax withheld on payments to certain countries. Tax-withheld amounts rose 59 percent and 38 percent from 1981 on income paid to Japan and the United Kingdom, respectively. These countries also had the largest percentage increases in income, although the order was reversed. The 59-percent tax-withheld increase for Japan was due to a 49-percent increase in income subject to withholding and a 3-percent decrease in exempt income. Tax-withheld amounts dropped substantially on payments to the Netherlands Antilles (51 percent) and the Netherlands (16 percent).

Effective Tax Rate by Country

Although the basic withholding tax rate is 30 percent, the actual rate can differ for a variety of reasons. Tax treaties allow for

lower tax rates on payments to certain countries. Income paid to exempt or government organizations is generally not taxed. Most U.S. income paid to foreign private foundations is taxed at 4 percent. In addition, income that is connected with the recipient's trade or business, and is therefore taxed as though it were received by a U.S. individual or organization, is not subject to withholding tax. Because of these factors, the effective U.S. withholding tax rate varies by country.

The following table shows the income paid, tax withheld by U.S. withholding agents, and the effective withholding tax rates for the 12 countries having the lowest effective tax rates. Only countries below the all-country average (7.1 percent) receiving at least 100 payments and \$1 million were considered.

Ranking of Effective Tax Rates
by Country, 1982

[Money amounts are in thousands]

Country	Gross income	Tax withheld	Effective tax rate
	(1)	(2)	(3)
Antigua	\$4,038	\$3	0.1%
Netherlands Antilles	1,580,359	13,069	0.8
Saudi Arabia	51,208	1,169	2.3
Finland	5,199	138	2.7
Trinidad and Tobago	1,797	52	2.9
Poland	2,561	76	3.0
Cayman Islands	43,876	1,970	4.5
West Germany	627,861	29,554	4.7
China (Taiwan)	9,055	451	5.0
Netherlands	1,463,583	73,848	5.0
Portugal	14,128	742	5.3
United Kingdom	2,174,506	136,097	6.3
All countries	10,624,310	758,186	7.1

Although all the countries have low U.S. effective withholding tax rates, the reasons vary for these low rates. Antigua and the Netherlands Antilles are "tax haven" countries (see "Tax Haven Countries") that have low tax-treaty rates on their U.S. source income [3]. Although Saudi Arabia is not a tax haven and does not receive the benefit of lower treaty rates, income paid to Saudi Arabian government organizations made up a substantial portion of all U.S. source Saudi income. An inordinately high proportion of Saudi investments in the United States is owned by the Saudi government. The income from these investments was not subject to U.S. withholding. Finland, Trinidad and Tobago, Poland, West Germany, and the United Kingdom are not generally considered tax havens, but have the benefit of low U.S. withholding tax rates due to tax treaties. One reason for the low (5 percent) effective tax rate for the

Netherlands is that the United States-Netherlands tax treaty allows for a 5-percent tax on dividends paid to Netherlands corporations that control or own the U.S. subsidiary. More than \$773 million of dividends paid to the Netherlands in 1982 fit this category. Ironically, many tax havens have above-average effective tax rates (see Figure B). This is generally because these countries have no tax treaties with the United States. The Cayman Islands is an exception, having an effective tax rate of 4.5 percent although it has no tax treaty with the United States.

Tax Haven Countries

A tax haven is generally considered to be a country having tax laws favorable to foreign individuals and organizations in an attempt to attract these investors. The tax haven country typically benefits by collecting certain fees or taxes (at a low tax rate). These foreign individuals and organizations would usually not invest in or through the tax haven if higher taxes were imposed. The most successful tax haven countries tend to have some or all of the following characteristics.

- o No withholding tax on most payments from the tax haven to foreign individuals and organizations,
- o Low or zero income tax rates for individuals or organizations within the tax haven country,
- o Secrecy laws to prevent foreign governments from obtaining financial information about their own citizens and organizations,
- o And finally, although most tax havens do not have this, tax treaties with low or zero withholding tax rates for most income payments received from foreign countries.

Recipients in tax haven countries tend to receive larger payments than in other countries. Figure B shows ten countries that qualify as tax havens to varying degrees. All but one of these countries received larger-than-average (\$18,800) payments. As in 1981, the Netherlands Antilles headed this list with an average payment of \$723,000, although this average is down from \$754,000 in that year.

Payments to tax haven countries are more likely to go to corporations in those countries than are payments to non-tax havens. This is primarily due to the predominance of financial corporations in tax havens. Many U.S. corporations have finance subsidiaries in these countries. Also, U.S. and foreign individuals and corporations may set up corporations in tax havens to avoid income taxes in their own country. Figure B shows the percentage of U.S. source income payments made to foreign corporations for ten selected tax haven countries. Each of the countries shown is above the 9-percent average for all countries. Antigua leads this list with a 74-percent figure.

The effective tax rate, defined as tax withheld divided by income paid, for the tax haven countries shown in Figure B, is affected by whether the country has a tax treaty with the United States. As was stated earlier, treaty countries tend to have lower effective tax rates than the nontreaty countries. Antigua, whose treaty with the United States is an extension of the United Kingdom treaty, had the lowest rate at 0.1 percent, followed by the Netherlands Antilles at 0.8 percent.

The Netherlands Antilles ranks high in the categories shown in Figure B, placing first, third, and second, respectively. Although no Gross National Product (GNP) information was available for the Netherlands Antilles for 1982, in 1981 U.S. source income was actually greater than the Antilles' GNP [4]. This U.S. source income, which was 93-percent interest, is inordinately high because large U.S. corporations borrow substantial amounts of money from foreign markets through their subsidiaries in the Antilles since this interest is exempt from withholding. It seems likely that recent legislation, which exempts most interest payments to all countries on new debt issues from tax withholding, will eliminate the need to borrow money through the Antilles. However, the United States provides many foreign governments with U.S. income information about their citizens and corporations. Therefore, foreign individuals and corporations wanting to avoid income tax in their own countries may still want these loans made through the Antilles for reasons of secrecy.

Tax Treaty Countries

Since payments to tax treaty countries are usually taxed at lower rates than payments to nontreaty countries, the effective tax rate for treaty country income is about one third the rate for nontreaty countries. The following table shows the income paid, tax withheld by U.S. withholding agents, and effective tax rates for both treaty country totals and nontreaty country totals.

Gross Income, Tax Withheld
and Effective Tax Rate

[Money amounts in thousands]

Country status	Gross income	Tax withheld	Effective tax rate
	(1)	(2)	(3)
All countries	\$10,624,310	\$758,186	7.1%
Treaty countries	10,012,968	650,143	6.5
Nontreaty countries	611,342	108,043	17.7

NOTE: More detailed information by country and treaty status is shown in Table 1.

Income paid to treaty countries rose by 12.6 percent from 1981 to 1982, while nontreaty countries received 26 percent less U.S. source income in 1982. It should be noted that tax treaties with three countries became effective during 1982. Therefore, Egypt, Malta and Morocco are included in the nontreaty country total for 1981 but in the treaty country total for 1982. Even with these additional countries included, tax withheld on payments to treaty countries rose only 5 percent. Nontreaty country tax withheld fell less than 1 percent despite the 26-percent drop in income.

Although lower tax treaty rates may reduce U.S. withholding tax revenue, this revenue loss is at least partly offset by lower foreign tax credits for U.S. individuals and corporations. Since tax treaties usually allow for correspondingly lower foreign withholding tax rates, U.S. individuals and corporations receiving income from tax treaty countries have less foreign tax withheld. This usually reduces their foreign tax credit and increases the amount of income tax paid to the United States.

Recipients in tax treaty countries, again, typically enjoy lower U.S. withholding tax rates. However, if the income is paid to a foreign nominee or fiduciary, additional withholding is often required and is collected by the government in the country of the nominee or fiduciary. The purpose of this additional withholding is to prevent citizens of nontreaty countries from taking advantage of the lower tax rates of treaty countries. The foreign government or withholding agent holds this additional tax until the ultimate recipient proves residency in that country. If residency is not proven within a certain period of time, the tax is remitted to the United States (see Table 1, column 7). In the case of Canada, nominees and fiduciaries act as withholding agents and remit this additional tax directly to the Internal Revenue Service (IRS).

Type of Income

As was stated earlier, interest income surpassed dividends as the most common type of income paid to nonresident aliens during 1982. This is due largely to U.S. corporations borrowing large amounts of money from foreign countries, where interest rates have been comparatively low. This interest is generally taxed at a low or zero rate when paid to recipients in treaty countries. This explains why tax withheld on interest represented only 20 percent of all tax, while interest income comprised 48 percent of all income. Conversely, tax withheld on dividend payments made up a considerably higher portion (71 percent) of all tax than dividend income represented of all income (43 percent). Figure C shows the percentage of total income paid and the percentage of total tax withheld for certain types of income.

Figure B.--Size of Average Payment, Percent of Payments to Corporations, and Effective Tax Rate, for Selected Tax Haven Countries, 1982¹

[Money amounts are in thousands]

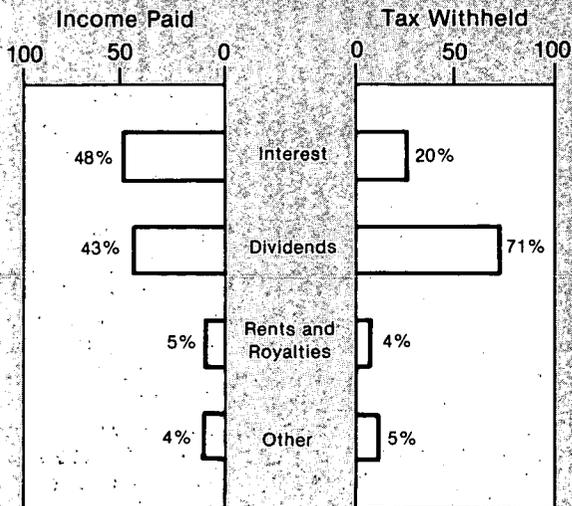
Country or geographic area	Size of payments		Percent of payments to corporations		Effective tax rate			
	Rank	Average	Rank	Percent	Rank	Gross Income	Tax Withheld ²	Percent
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Netherlands Antilles	1	\$723	3	52%	2	\$1,580,359	\$13,069	0.8%
Netherlands	2	143	11	17	10	1,463,583	73,848	5.0
British Virgin Islands ..	4	69	4	39	31	32,186	4,502	14.0
Cayman Islands	5	60	2	62	7	43,876	1,970	4.5
Bermuda	6	58	10	21	50	72,277	16,348	22.6
Switzerland	7	57	12	15	24	1,176,462	121,429	10.3
Panama	11	26	5	30	44	69,624	15,018	21.6
Luxembourg	12	25	7	27	15	73,117	5,388	7.4
Antigua	14	20	1	74	1	4,038	3	0.1
Bahamas	16	17	6	29	60	31,283	8,393	26.8

¹Countries considered for ranking purposes include only those receiving 100 or more payments and \$1 million or more for all recipients for "Size of Payments" and "Effective Tax Rate" columns. The same restrictions were applied to "Percent of Payments to Corporations" but for corporate recipients only.

²Tax withheld by domestic withholding agents only.

Figure C

Percent of Total Income Paid and Percent of Total Tax Withheld, by Income Type, 1982



Tax withheld on interest rose at the same rate (60 percent) as the interest payments from 1981 to 1982. Tax withheld on dividends rose by 9 percent in the same period. Even with this rapid increase in tax on interest, the tax withheld on dividends was more than three and a half times greater.

Type of Recipient

As in 1981, foreign corporations received the majority (70 percent) of all U.S. source income, although this figure is down slightly from the 73 percent figure of that year. Foreign individuals received just 7 percent of all income although they received 73 percent of all payments. Payments to individuals were far smaller on the average (\$1,800) than payments to corporations (\$144,000). Tax withheld by U.S. withholding agents on payments to individuals represented 14 percent of all tax. This is double the percentage shown earlier for individual income as a percent of all income. This disparity exists because a greater percentage of income paid to individuals is subject to withholding (71 percent) than for all recipients (56 percent). Conversely, foreign corporations, which had only 51 percent of their U.S. source income subject to withholding, received 73 percent of all income, while tax withheld on payments to corporations made up just 70 percent of all tax.

The various types of recipients not only received different amounts of U.S. income, but also tended to receive different kinds of income. As is shown in Figure D, 54 percent of U.S. source income paid to foreign corporations was interest income. The corresponding figure for foreign individuals was only 21 percent. A higher percentage of income of individuals was made up of dividends (45 percent) than the income of corporations (38 percent). More than 80 percent of nominee and fiduciary income was dividends while government, international, and exempt organizations tended to receive interest (58 percent). Although personal service income is not shown as a specific category in Figure D, 13 percent of the income paid to foreign individuals falls into this category. Almost 90 percent of all personal service income was paid to individuals.

U.S. Withholding Taxes and Foreign Withholding Taxes

Most foreign countries impose withholding taxes similar to those of the United States. U.S. individuals and organizations that receive income from foreign countries can usually take a tax credit for the foreign taxes withheld from this income. Although foreign withholding tax rates tend to be similar to the U.S. tax rates, foreign countries, in general, withhold far more total tax on payments to U.S. corporations than the United States withholds on similar payments to foreign corporations. Although similar data dealing with the amount of income paid are not available, this withholding tax disparity is probably mainly due to U.S. corporations receiving more foreign income than foreign corporations receive U.S. income. In 1980, the latest year for which such information is available, U.S. corporations claiming a foreign tax credit had \$2.6 billion of tax withheld on dividends, interest, rents and royalties received from foreign countries [5]. This was more than seven times the amount of tax the U.S. withheld (\$362.8 million) on similar payments to foreign countries. This \$2.6 billion of foreign taxes withheld does not include tax withheld on payments to U.S. corporations that did not claim a foreign tax credit.

Figure E shows U.S. tax withheld on payments to foreign corporations, foreign taxes withheld on foreign income received by U.S. corporations claiming a foreign tax credit, and U.S. tax surplus or deficit (U.S. tax withheld minus foreign tax withheld) by income type by country for 1980. More tax was withheld by foreign countries than by the United States for each of the income categories (dividends, interest, and rents, royalties and license fees) shown.

Foreign tax withheld on dividend payments to U.S. corporations exceeded similar U.S. tax on dividend payments to foreign corporations by almost \$1.1 billion. One possible reason for

this disparity is that U.S. corporate investment in foreign corporations is probably greater than the reverse. It is also possible that foreign corporations are more likely to invest in the United States through unincorporated branches to avoid withholding taxes. These corporations would still pay U.S. income tax on their U.S. income. As the United States tends to have a relatively stable economy, foreign corporations may accept lower profit margins in the United States and therefore receive lower dividends, in exchange for a secure U.S. investment. U.S. investors in less-secure foreign economies, having greater political, and therefore economic, risk may require higher profit margins and therefore receive greater dividends from their foreign subsidiaries.

Foreign governments also withheld far more tax on interest payments to U.S. corporations than the United States withheld on similar payments to foreign corporations during 1980. The disparity is smaller (\$607 million) than for dividends and more than 57 percent of this difference can be accounted for by two countries, Mexico and Brazil. These countries are heavily indebted to U.S. banks and therefore must pay large interest amounts which are subject to foreign tax withholding. Tax withheld on interest payments to U.S. banks (\$309 million) represented 88 percent of tax withheld by Mexico and Brazil on interest payments to all U.S. corporations.

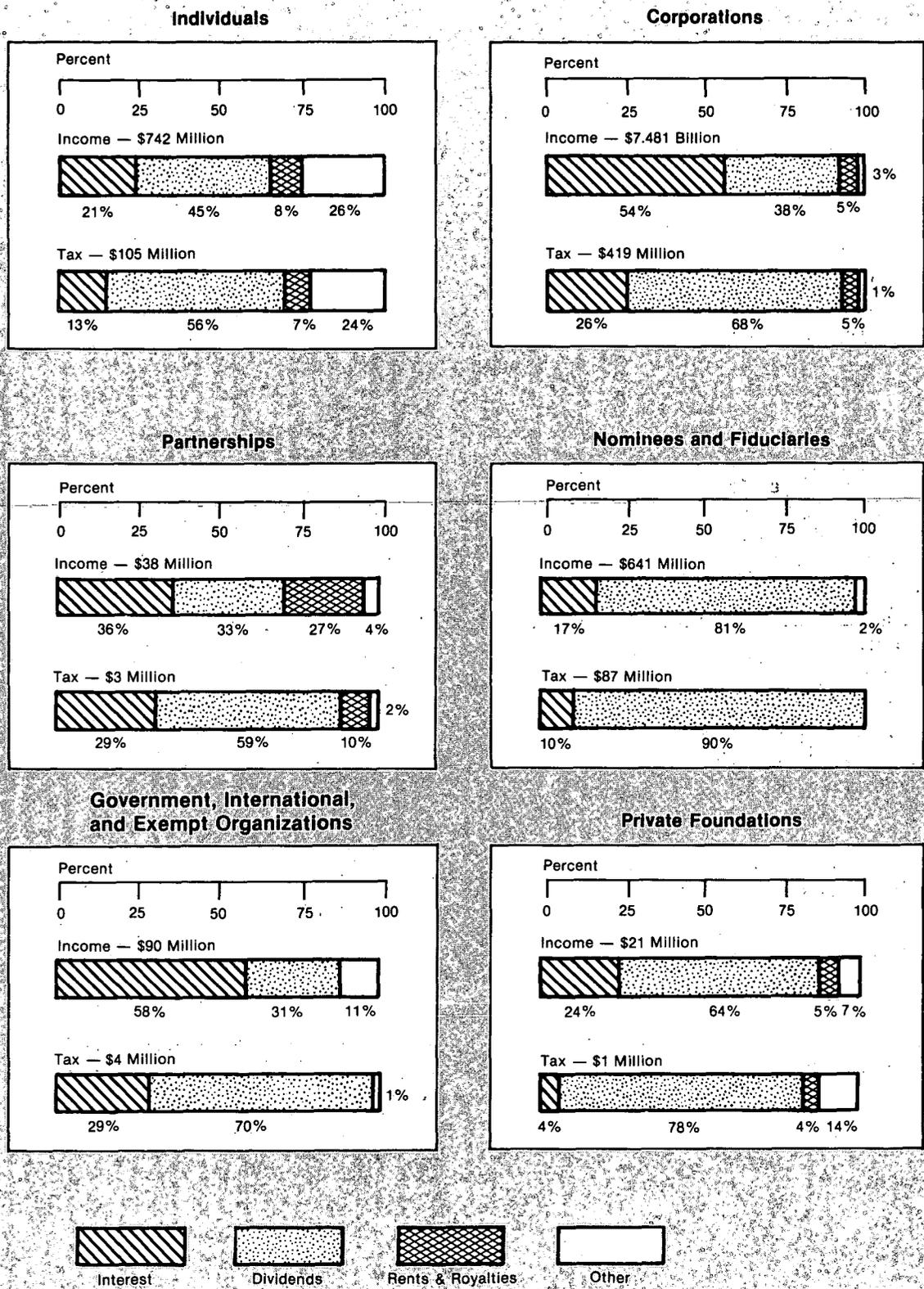
SUMMARY

The Deficit Reduction Act of 1984 exempts from withholding tax most U.S. source interest payments to nonresident aliens on new loans. This will enable small companies and the U.S. Treasury to borrow money from foreign lenders, whose interest rates have typically been lower than those in the United States. Large U.S. borrowers, who previously issued substantial foreign debt through Netherlands Antilles subsidiaries to avoid this withholding tax, can now issue this debt directly to the country of the lender. This may lessen the Antilles status as a tax haven.

Income payments to the United Kingdom increased by 60 percent from 1981 to 1982, from almost \$1.4 billion to more than \$2.2 billion. This increase is due in part to "dual resident corporations" making interest payments to U.K. lenders for startup borrowing costs and general debt. These "dual resident corporations" are incorporated in the United States while keeping their management in the United Kingdom. This dual residency allows the corporations to deduct losses from income in both countries.

For the first time interest has surpassed dividends as the most common type of income paid to nonresident aliens. Interest accounted for 48 percent of such income while dividends fell from 1981, to 43 percent of all income.

Figure D
Percent of Income Paid by Income Type and Percent of Tax Withheld by Income Type, by Recipient Type, 1982



Interest
 Dividends
 Rents & Royalties
 Other

Figure E.--U.S. Tax Withheld on Payments to Foreign Corporations, Foreign Tax Withheld on Payments to U.S. Corporations Claiming a Foreign Tax Credit, and U.S. Tax Surplus or Deficit, by Income Type and Country, 1980

[Money amounts are in thousands]

Country or geographic area	Tax withheld on dividends			Tax withheld on interest			Tax withheld on rents, royalties and license fees		
	U.S. payments to foreign corporations ¹	Foreign payments to U.S. corporations ²	U.S. tax surplus or deficit	U.S. payments to foreign corporations ¹	Foreign payments to U.S. corporations ²	U.S. tax surplus or deficit	U.S. payments to foreign corporations ¹	Foreign payments to U.S. corporations ²	U.S. tax surplus or deficit
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
All countries	\$275,165	\$1,373,863	-\$1,098,698	\$69,752	\$675,488	-\$606,736	\$17,786	\$547,938	\$-530,152
Argentina	192	28,828	-28,636	10	38,711	-38,701	12	12,071	-12,059
Australia	343	55,062	-54,719	272	8,474	-8,202	955	72,761	-71,806
Belgium	4,189	42,770	-38,581	4,330	4,573	-243	2	268	-266
Brazil	16	84,386	-84,370	149	148,116	-147,967	15	19,556	-19,541
Canada	28,544	236,365	-207,821	22,234	111,923	-89,689	3,503	83,033	-79,530
France	17,475	24,859	-7,384	3,515	3,237	+278	1,771	25,836	-24,065
Italy	756	29,473	-28,717	206	3,963	-3,757	-	19,492	-19,492
Japan	17,501	51,526	-34,025	11,795	11,215	+580	6,351	77,917	-71,566
Mexico	419	53,037	-52,618	190	201,816	-201,626	774	77,539	-76,765
Netherlands	56,426	52,908	+3,518	1,494	3,310	-1,816	8	231	-223
Netherlands Antilles	4,668	4,048	+620	1,611	154	+1,457	17	7	+10
South Africa	44	36,890	-36,846	10	290	-280	6	10,085	-10,079
South Korea	5	27,163	-27,158	4	56	-52	-	1,713	-1,713
Switzerland	61,126	48,238	+12,888	11,111	534	+10,577	75	1,336	-1,261
Venezuela	310	20,056	-19,746	122	26,893	-26,771	2	5,556	-5,554
United Kingdom	45,149	183,235	-138,086	632	10,522	-9,890	711	10,964	-10,253
West Germany	5,829	255,766	-249,937	62	748	-686	5	1,685	-1,680
Other	32,173	139,253	-107,080	12,005	101,953	-89,948	3,579	127,888	-124,309

¹Does not include tax remitted by foreign governments and withholding agents as these amounts cannot be allocated to specific years.
²Does not include tax withheld on income received by U.S. corporations not claiming a foreign tax credit. The amounts shown are for corporation tax returns having accounting periods ending between July 1980 and June 1981.

Although most payments went to individuals, the majority of the total income was paid to foreign corporations. Other types of recipients such as partnerships, fiduciaries, nominees, government organizations, exempt organizations, and private foundations received both a small percentage of all payments and a small percentage of the total income.

The United States collects far less in withholding taxes on payments to nonresident aliens than foreign countries withhold on similar payments to the United States. The withholding tax disparity for dividend income is probably due to the continuing high level of U.S. multinational investment in foreign countries. This subjects the dividend payments to the U.S. parent to foreign withholding. A slightly smaller disparity exists for interest payments. More than half the withholding tax on interest claimed by U.S. corporations for foreign tax credit purposes was withheld by Brazil and Mexico. These countries impose withholding taxes on the interest portion of the repayment of large borrowings from U.S. banks.

CHANGES TO 1981 FORM 1042S DATA

The following corrections were made to the 1981 Form 1042S data published in the Summer 1983 issue of the Statistics of Income Bulletin. These income changes are reflected in all text and tables of this article utilizing or

referring to 1981 data. No changes were made to tax data. Amounts are in thousands of dollars.

	Original amount	Adjustment	Revised amount
	(1)	(2)	(3)
Country			
All countries	\$9,561,489	\$155,498	\$9,716,987
Canada	1,238,255	-21,000	1,217,255
France	650,496	2,000	652,496
Netherlands	1,339,633	200,000	1,539,633
Switzerland	1,203,878	-2,000	1,201,878
West Germany	621,556	-23,502	598,054
Income type			
All income	\$9,561,489	\$155,498	\$9,716,987
Dividends	4,268,729	173,498	4,442,227
Other	5,292,760	-18,000	5,274,760
Recipient type			
All recipients	\$9,561,489	\$155,498	\$9,716,987
Individuals	733,383	-16,000	717,383
Corporations	7,017,018	198,000	7,215,018
Fiduciaries	68,088	2,000	70,088
Nominees	328,769	-5,000	323,769
Unknown	677,223	-23,052	654,171

DATA SOURCES AND LIMITATIONS

Payors of income to nonresident aliens must withhold tax in accordance with Chapter 3 of the Internal Revenue Code. The Form 1042S is filed to report this income and the U.S. tax withheld. Often the payor has a financial institution act as withholding agent.

The present statistics are tabulated by calendar year, based on all Forms 1042S filed for 1982. The years indicated in the tables represent the year in which the income was paid and the U.S. tax withheld, except for the tax from foreign governments and withholding agents. These amounts are shown by the year the tax was remitted to the United States under treaty agreements. Tax withheld amounts and percentages shown in Table 2 and Figures B, C, D and E, do not include tax withheld by foreign governments and withholding agents (except Canada). This additional withholding cannot be properly attributed to specific recipient and income types. Definitions and other information are available in the IRS Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Corporations.

As all Forms 1042S are included in these statistics, they were not subject to sampling error. However, the data are subject to non-sampling errors such as computer data entry errors and minor taxpayer reporting errors. Forms 1042S with income greater than \$500,000 were manually verified. A limited computerized program was used to test the data for certain basic numerical relationships, including the calculation of the correct tax withheld.

More detailed information on nonresident alien income and tax is available from the Statistics of Income (SOI) Division. This includes information for types of income and countries not discussed in this article.

EXPLANATION OF TERMS

Income Effectively Connected With a Trade or Business.--Income that is effectively connected with the conduct of a trade or business in the United States is exempt from withholding. This income is subject to substantially the same tax rates that apply to U.S. citizens, residents, and corporations. For example, if a foreign corporation has unincorporated operations in the United States, a Form 1120F must be filed and appropriate taxes paid for the income of

this operation. When income is then remitted to the foreign corporation, it is considered connected with a U.S. trade or business and not retaxed.

Nominee.--An entity, chosen or appointed to accept income for, or act on behalf of, the eventual recipient of the income. Typically a financial institution acts as nominee.

Nonresident Alien.--For purposes of this article, a nonresident alien is defined as an individual whose residence is not within the United States and who is not a U.S. citizen. Corporations and other organizations created or organized outside the United States are also considered nonresident aliens.

Withholding Agent.--Any person (individual, corporation, partnership, estate, or trust) required to withhold tax. Usually the withholding agent is the payor of the income or a "person" (usually a financial institution) acting on behalf of the payor. A foreign nominee or fiduciary required to withhold additional tax under a tax treaty is also a withholding agent.

NOTES AND REFERENCES

- [1] Phillips, John S., "Dual Resident Corporations," International Tax Review, Price Waterhouse, Vol. 9, No. 4, p. 2.
- [2] Certain data published for 1981 in the Statistics of Income Bulletin Summer 1983, were later adjusted. See "Changes to 1981 Form 1042S Data" in this article.
- [3] Treaties have been terminated with the following countries as of January 1, 1984: Anguilla, Barbados, Belize, Dominica, Grenada, Montserrat, St. Christopher-Nevis, St. Lucia, St. Vincent and the Grenadines. Antigua and Barbuda terminated its treaty with the United States effective August 26, 1983.
- [4] Carson, Chris R., "Nonresident Alien Income and Tax Withheld, 1981," Statistics of Income Bulletin, Summer 1983, pp. 36-37.
- [5] For additional information on foreign withholding taxes by income type and country, see the Foreign Tax Credit article in the upcoming Statistics of Income Bulletin, Winter 1984-1985.

Table 1.--Number of Forms 1042S Filed, Gross Income Paid, Tax Withheld, and Other Items, by Selected Treaty and Nontreaty Countries, 1982

[Money amounts are in thousands of dollars]

Country or Geographic area	Number of Forms 1042S filed	Income paid			Tax withheld		
		Total	Exempt from withholding	Subject to withholding	Total	Domestic withholding agents	Foreign Governments and withholding agents
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Total.....	565,091	10,624,310	4,672,184	5,952,126	848,874	758,186	90,688
Treaty country, total.....	476,469	10,012,968	4,472,778	5,540,190	740,831	650,143	90,688
Australia.....	10,311	26,577	7,072	19,505	4,019	4,019	-
Austria.....	3,218	12,081	4,842	7,239	1,238	1,238	-
Belgium.....	8,633	120,166	23,781	96,385	16,485	15,050	1,435
Canada.....	241,256	1,151,846	423,631	728,215	110,385	110,385	-
Denmark.....	1,670	10,582	3,614	6,968	1,018	1,006	12
France.....	13,420	660,975	181,680	479,295	52,153	51,487	666
Germany, Federal Republic....	45,042	627,861	436,673	191,188	29,554	29,554	-
Greece.....	3,651	7,177	2,898	4,279	1,157	1,157	-
Ireland.....	3,529	15,140	5,956	9,184	1,428	1,428	-
Italy.....	6,863	51,748	19,300	32,448	7,565	7,565	-
Japan.....	6,120	703,643	136,245	567,398	61,661	61,661	-
Luxembourg.....	2,968	73,117	48,071	25,046	6,849	5,388	1,461
Netherlands.....	10,224	1,463,583	448,030	1,015,553	74,211	73,848	363
Netherlands Antilles.....	2,185	1,580,359	1,511,892	68,467	13,078	13,069	9
Norway.....	3,167	11,567	3,538	8,029	1,009	1,009	-
South Africa.....	2,044	4,071	576	3,495	1,045	1,045	-
Sweden.....	4,762	73,824	15,234	58,590	5,338	5,338	-
Switzerland.....	20,568	1,176,462	200,946	975,516	206,429	121,429	85,000
United Kingdom.....	76,927	2,174,506	975,440	1,199,066	142,468	140,726	1,742
Other treaty countries.....	9,911	67,683	23,359	44,324	3,741	3,741	-
Nontreaty country, total.....	88,622	611,342	199,406	411,936	108,043	108,043	-
Argentina.....	3,823	11,533	4,335	7,198	2,079	2,079	-
Bahamas.....	1,814	31,283	1,878	29,405	8,393	8,393	-
Bermuda.....	1,236	72,277	12,878	59,399	16,348	16,348	-
Brazil.....	1,738	7,506	959	6,547	1,900	1,900	-
Cayman Islands.....	736	43,876	37,231	6,645	1,970	1,970	-
Hong Kong.....	9,133	35,999	3,642	32,357	9,577	9,577	-
Israel.....	3,529	15,640	5,956	9,684	1,741	1,741	-
Kuwait.....	743	4,795	1,191	3,605	1,075	1,075	-
Liechtenstein.....	772	15,150	2,199	12,951	3,924	3,924	-
Mexico.....	8,863	30,601	7,079	23,522	6,888	6,888	-
Panama.....	2,710	69,624	18,781	50,843	15,018	15,018	-
Portugal.....	888	14,128	679	13,449	742	742	-
Saudi Arabia.....	2,298	51,208	47,257	3,950	1,169	1,169	-
Spain.....	3,555	17,344	5,833	11,511	3,150	3,150	-
United Arab Emirates.....	549	1,340	564	777	233	233	-
Venezuela.....	4,814	11,774	4,260	7,513	2,217	2,217	-
Other nontreaty countries....	41,421	177,264	44,684	132,580	31,619	31,619	-

NOTE: Detail may not add to total because of rounding.

Nonresident Alien Income and Tax, 1982

Table 2.--Number of Forms 1042S Filed, Tax Withheld, and Gross Income Paid by Selected Income Type, by Selected Recipient Type and Selected Country of Recipient, 1982

[Money amounts are in thousands of dollars]

Country or Geographic area	Number of Forms 1042S filed	Tax withheld	Income paid				
			Total	Interest	Dividends	Rent and royalty	Personal service
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
ALL RECIPIENTS							
Total.....	565,091	758,186	10,624,310	5,134,841	4,546,634	510,898	97,698
Bahamas.....	1,814	8,393	31,283	5,831	22,885	614	100
Belgium.....	8,633	15,050	120,166	38,184	64,111	15,555	746
Bermuda.....	1,236	16,348	72,277	31,550	24,084	6,104	468
Canada.....	241,256	110,385	1,151,846	503,340	503,497	53,676	10,074
Cayman Islands.....	736	1,970	43,876	37,731	5,021	301	77
France.....	13,420	51,487	660,975	265,539	274,687	47,847	8,075
Germany, Federal Republic.....	45,042	29,554	627,861	391,450	160,404	46,088	6,274
Hong Kong.....	9,133	9,577	35,999	4,105	29,445	1,600	605
Italy.....	6,863	7,565	51,748	16,937	12,377	14,160	3,291
Japan.....	6,120	61,661	703,643	433,329	140,400	108,090	7,916
Luxembourg.....	2,968	5,388	73,117	38,240	33,975	2	27
Mexico.....	8,863	6,888	30,601	7,773	8,749	6,326	2,200
Netherlands.....	10,224	73,848	1,463,583	423,272	994,663	29,742	2,672
Netherlands Antilles.....	2,185	13,069	1,580,359	1,470,529	70,715	31,939	51
Panama.....	2,710	15,018	69,624	36,896	27,236	3,453	94
Saudi Arabia.....	2,298	1,169	51,208	36,842	2,983	25	173
Sweden.....	4,762	5,338	73,824	8,400	55,303	1,146	5,621
Switzerland.....	20,568	121,429	1,176,462	433,681	693,283	37,344	3,420
United Kingdom.....	79,049	136,097	2,174,506	820,170	1,197,648	86,580	21,407
Other countries.....	97,211	67,952	431,352	131,042	225,168	20,306	24,407
INDIVIDUALS							
Total.....	413,854	105,333	742,145	152,237	335,004	62,342	86,797
Bahamas.....	832	1,018	3,815	344	3,143	212	75
Belgium.....	7,019	1,006	7,777	812	4,553	179	726
Bermuda.....	706	586	2,123	213	883	35	417
Canada.....	183,020	16,923	136,714	23,100	65,718	12,760	7,730
Cayman Islands.....	112	135	515	109	364	42	-
France.....	9,720	4,655	36,897	6,243	12,822	4,916	7,417
Germany, Federal Republic.....	37,110	6,877	89,514	20,573	49,662	4,337	5,859
Hong Kong.....	7,527	4,465	16,425	926	14,146	662	555
Italy.....	5,787	5,379	25,716	2,074	4,326	11,439	3,095
Japan.....	4,249	1,533	16,773	2,513	2,974	448	6,611
Luxembourg.....	849	260	1,400	113	1,197	2	10
Mexico.....	8,017	4,372	20,211	4,322	6,712	4,867	2,038
Netherlands.....	5,278	2,500	22,894	2,031	13,303	3,901	2,114
Netherlands Antilles.....	492	729	10,208	5,674	3,953	396	29
Panama.....	1,496	1,807	6,898	1,431	5,177	29	9
Saudi Arabia.....	2,088	750	7,624	274	1,788	25	173
Sweden.....	4,247	2,105	10,896	510	2,093	182	5,552
Switzerland.....	9,175	8,057	62,047	20,272	34,914	1,942	2,502
United Kingdom.....	42,718	12,155	108,651	25,871	44,093	8,976	19,581
Other countries.....	83,412	30,021	155,047	34,832	63,183	6,992	22,304
CORPORATIONS							
Total.....	51,962	419,079	7,481,441	4,039,602	2,831,605	393,570	8,617
Bahamas.....	526	3,948	15,078	3,839	9,115	393	17
Belgium.....	570	8,124	73,201	32,965	24,873	15,319	-
Bermuda.....	253	10,317	51,106	30,447	9,825	1,350	19
Canada.....	22,347	52,670	680,799	396,035	204,248	31,628	2,064
Cayman Islands.....	453	866	36,661	34,056	1,834	257	63
France.....	974	19,921	388,161	156,820	135,165	37,135	352
Germany, Federal Republic.....	1,853	15,802	352,747	238,885	68,645	34,365	413
Hong Kong.....	627	3,713	13,933	2,870	10,331	576	50
Italy.....	265	1,462	20,581	13,540	4,495	2,403	45
Japan.....	1,449	54,567	635,677	406,099	117,498	104,520	1,273
Luxembourg.....	799	2,362	40,470	31,262	9,147	-	-
Mexico.....	314	1,765	6,895	2,071	1,076	1,188	12
Netherlands.....	1,740	53,038	1,274,152	397,252	848,583	24,725	552
Netherlands Antilles.....	1,145	9,175	1,430,131	1,347,845	45,785	29,609	5
Panama.....	804	6,744	36,062	18,227	14,861	2,287	85
Saudi Arabia.....	33	69	229	172	57	-	-
Sweden.....	198	2,764	54,716	7,147	46,553	758	37
Switzerland.....	3,154	73,453	773,533	326,179	409,441	32,636	893
United Kingdom.....	9,460	74,261	1,418,293	515,561	799,540	64,518	1,743
Other countries.....	4,998	24,058	179,016	78,330	70,533	9,903	994