

July 27, 2004

Protocol Amending the United States Income Tax Treaty with Barbados May Affect Many Offshore Companies with U.S. Operations

On July 14, 2004, the United States and Barbados signed a Protocol amending the United States income tax treaty with Barbados (the "Treaty") that will enter into force upon the exchange of instruments of ratification. It is unclear at the present time when ratification will occur.

A number of offshore companies with U.S. operations have used a Barbadian holding company formed as an International Business Company as an intermediate entity in order to reduce the group's overall tax liability.

The Treaty currently provides for a reduction in the U.S. 30 percent withholding tax on dividends, interest, royalties and other income if paid to a Barbadian company entitled to the benefits of the Treaty, as well as other tax benefits. Consequently, for example, a Barbadian International Business Company that qualifies for Treaty benefits would be entitled to a reduction in the U.S. withholding tax from 30 percent to five (5) percent with respect to dividends paid from its wholly owned U.S. subsidiaries.

The Protocol, however, tightens the rules with respect to eligibility for Treaty benefits, rendering many companies eligible for Treaty benefits under the existing Treaty as ineligible. Even if a Barbadian company otherwise would qualify as eligible for Treaty benefits, the Protocol provides that persons entitled to income tax benefits under the provisions of a special tax regime (i.e., a regime that provides for an effective rate of tax substantially lower than the generally applicable rate for such person) will not be entitled to Treaty benefits with respect to dividends, interest and royalties. Thus, for example, a Barbadian holding company formed as an International Business Company and, accordingly, subject to a rate of Barbadian tax of two and one half (2.5) percent or less, would generally not be eligible for a reduction of the 30 percent U.S. federal withholding tax rate on dividends paid to it by its wholly owned U.S. subsidiaries.

Offices worldwide

New York
Washington, D.C.
Albany
Boston
Harrisburg
Hartford
Houston
Jacksonville
Los Angeles
Newark
Pittsburgh
Salt Lake City
San Francisco

London
a multinational partnership
Paris
Brussels
Johannesburg
(Pty) Ltd.
Moscow
Riyadh
affiliated office
Bishkek
Almaty
Beijing

www.llgm.com