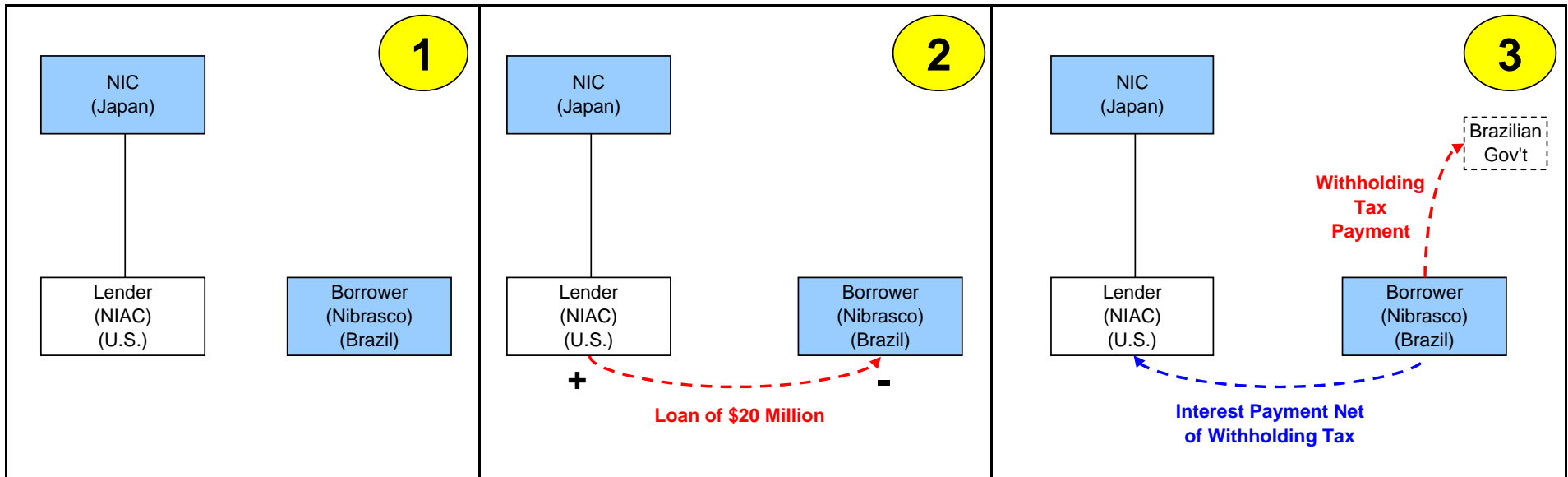


**Foreign Tax Credits:  
 Legal Liability for Withholding Taxes**

**Initial Structure**

**Loan**

**Payment of Interest  
& Withholding Tax**



The case involved several issues related to foreign tax credits. This tax chart only addresses the first issue in the case -- whether the lender was legally liable for Brazilian withholding taxes paid by the Brazilian borrower. The Tax Court held that the lender was liable. The following is an excerpt from the case:

Section 901 allows a domestic corporation to claim as a credit against its Federal income tax . . . the amount of any income taxes paid on behalf of the taxpayer to a foreign country . . . .

A foreign tax is creditable only if the taxpayer is legally liable under foreign law for the tax. . . . However, legal liability for a tax and the obligation to pay the tax are not necessarily the same. For example, under a withholding system, legal liability for the tax and the obligation to pay the tax are different. The Federal wage withholding system illustrates this difference--the employer is the person obligated to withhold the tax and to pay the withheld tax to the Government; the employee is the person legally liable for the tax. . . .

U.S. tax law is the standard for deciding whether a foreign levy is a creditable income tax. *Biddle v. Commissioner*, 302 U.S. 573 (1938). After reviewing translations of the applicable Brazilian law, it is our opinion that the tax is on the receipt of the interest. The tax is imposed on the foreign lender; the Brazilian borrower is simply the person required to pay the tax on behalf of the foreign lender. . . .