



Market Commentary
June 20th, 2025

English Version

Insigneo Weekly Dispatch

Understanding the Potential Effects of Section 899

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Understanding the Potential Effects of Section 899

What is Section 899? In essence, Section 899 is a tax on certain income received by companies and investors from countries deemed to carry out unfair practices on taxes paid by U.S. persons or businesses, known as “discriminatory foreign countries”.

Who could be affected? Foreign corporations, entities, or individuals that are incorporated or are citizens of a country classified as a “discriminatory foreign country”, who receive certain forms of income generated in the United States could be affected by Section 899.

What are the possible effects of Section 899? In essence, if approved, Section 899 would make foreign recipients of certain income generated in the U.S. subject to higher taxes, if these recipients reside in a country designated as a “discriminatory foreign country”.

The current administration’s One Big Beautiful Bill Act is designed to make a number of tax cuts permanent, as well as changing portions of the United State’s tax code. As it stands, the bill has received House approval and is currently being reviewed by the Senate. The impetus behind the bill is to promote economic and income growth in the country by reducing certain taxes and modifying others. However, the Big Beautiful Bill may prove not to be beautiful for everyone. One section of the bill that has been making news in the financial arena is known as Section 899, which we review in more detail below.

What is Section 899? In essence, Section 899 is a tax on certain income received by companies and investors from countries deemed to carry out unfair practices on taxes paid by U.S. persons or businesses, known as “discriminatory foreign countries”. What makes a country “discriminatory” is the implementation of what the government recognizes as unfair foreign taxes, which mainly fall under three categories: Undertaxed Profits Rule (UTPR), Diverted Profit Taxes (DPT), and Digital Services Tax (DST). UTPR and DPT are designed to prevent companies from shifting profits to jurisdictions with lower taxes in order to lower their tax liabilities. DST is a tax imposed by certain countries on the revenues of large, multinational corporations that provide digital services such as e-commerce or online advertising.

Who could be affected? Foreign corporations, entities, or individuals that are incorporated or are citizens of a country classified as a “discriminatory foreign country”, who receive certain forms of income generated in the United States could be affected by Section 899. The main countries that could be considered to be “discriminatory foreign countries” under these rules would most likely be: Austria, Belgium, Bulgaria, Canada, Croatia, Cyprus, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Luxembourg, Netherlands,

New Zealand, Norway, Poland, Portugal, Romania, Slovenia, South Korea, Spain, Sweden, Thailand, Turkey, and the UK. However, certain countries in Latin America such as Argentina, Colombia, Paraguay, and Uruguay implement a form of Digital Services Tax and could potentially fall into the “discriminatory foreign country” category. Although Mexico does not implement a DST, it does implement a Value Added Tax (VAT) on certain digital services. However, it remains unclear whether this form of tax would qualify under the premises of Section 899.

What are the possible effects of Section 899? In essence, if approved, Section 899 would make foreign recipients of certain income generated in the U.S. subject to higher taxes, if these recipients reside in a country designated as a “discriminatory foreign country”. The proposed mechanism would increase taxes by 5% in the first year, then 5% each year with a maximum cap of 20%. For example, if a foreign citizen is subject to a 30% withholding tax on dividends from a U.S. company, the new withholding tax would be 35% in the first year, increasing by 5% each subsequent year, until it reaches a maximum of 50%. This would apply to U.S. generated income such as dividends, interest, royalties, and income connected

to real estate properties, as well as subsidiary or branch revenues of foreign corporations. If the bill remains in its current form, capital gains will continue to remain exempt from taxes. It is important to note that interest on U.S. government and corporate bonds and deposits is also expected to remain exempt. Additionally, personal remittances such as money transfers sent from the U.S. to families abroad are also expected to remain unaffected.

It is important to remember that the proposed tax bill has yet to be approved by the Senate. If approved, portions of the bill, including Section 899, could be modified or delayed for a number of years. As a result, the situation remains fluid, and the final form and effects of this proposed legislation remain unknown. We will continue to monitor the situation and will continue to keep you informed with any new developments. ■



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