

Guide to US tax terms

Tax concepts

US tax	Definition	Tax consequences	Relevant investors	Relevant investments
Effectively connected income (“ ECI ”)	ECI is all income from sources within the US connected with the conduct of trade or business that a non-US person engages in.	If a non-US investor receives ECI either directly or through a tax transparent entity (or one that is treated as tax transparent for US persons) it will be required to file a tax return and pay tax in the US.	Non-US investors	US operating businesses including certain direct lending strategies
Foreign investment in Real Property Tax Act (“ FIRPTA ”)	FIRPTA applies when there is a disposition of a US real property interest (as defined below).	The transferee must deduct and withhold tax on the total amount realised by the non-US investor on the disposition of a US real property interest.	Non-US investors	US or non-US businesses holding US real property
US real property interests (“ USRPI ”)	A US real property interest is an interest, other than as a creditor, in: <ul style="list-style-type: none"> – real property located in the US and personal property associated with the use of real property; OR – any corporation (including both US companies and non-US companies) that is a US real property corporation (as defined below) during the shorter period during which the interest was held, or the 5 year period ending on the date of disposition. 	FIRPTA may apply.	Non-US investors	US or non-US businesses with US real property
Unrelated business taxable income (“ UBTI ”)	UBTI is income from: <ul style="list-style-type: none"> – a trade or business; – regularly carried on by a tax exempt organisation; which is not substantially related to the organisation’s tax-exempt purpose. 	If a US tax exempt investor (other than a Super Tax Exempt investor) receives UBTI directly or through a tax transparent entity (or one that is treated as tax transparent for US purposes) it will be subject to tax at the rate applicable to corporations.	US tax exempt investors	Operating businesses (and in some cases acquisition financing (known as UDFI))
Commercial activity income (“ CAI ”)	Sovereign wealth funds (known as 892 investors in the US) benefit from a special tax regime in the US found in section 892 of the Code. Section 892 of the Code provides that sovereign wealth	Sovereign wealth funds which meet the regulatory definition of a “foreign government” benefit from certain exemptions from US tax.	Sovereign wealth funds (892 investors)	Income derived by a sovereign wealth fund from the conduct of a commercial activity

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	<p>funds will not be taxed in the US. However, this exemption does not apply to CAI.</p> <p>CAI means income derived by a sovereign wealth fund from the conduct of a commercial activity (with the exception of trading or investment), income received directly or indirectly from a “commercially controlled entity” and any gain derived from the disposition of any interest in a “commercially controlled entity”.</p> <p>A “commercially controlled entity” can be defined as any separate entity (corporation or partnership) engaged in a commercial activity in any part of the world in which the foreign government holds directly or indirectly a greater than 50 per cent interest in the votes, value or control of such entity. Any income generated in the US by such a commercially controlled entity loses exemption under section 892.</p>	<p>The exemptions are not available for CAI so sovereign wealth funds would become subject to US tax.</p>		<p>(with the exception of trading or investment), income received directly or indirectly from a “commercially controlled entity” and any gain derived from the disposition of any interest in a “commercially controlled entity”</p>
<p>Passive foreign investment company (“PFIC”)</p>	<p>A PFIC is a non-US company where:</p> <ul style="list-style-type: none"> – 75% or more of its gross income is “passive income” (which generally includes dividends, interest, royalties, rents and annuities); or – the average percentage of assets held by such corporation produce or are held for the production of passive income is at least 50%. <p>A PFIC can be a QEF (see below).</p>	<p>If a US investor is treated as owning an interest in a PFIC, that person may be subject to special tax and interest charges which approximate the US federal income tax charge that would have been payable if the foreign corporation had distributed all of its income every year.</p>	<p>US investors</p>	<p>Non-US companies</p>
<p>Qualified electing fund (“QEF”)</p>	<p>A PFIC is a QEF if a US person who is a direct or indirect shareholder (the “US Shareholder”) of the PFIC elects to treat the PFIC as a QEF and complies with certain requirements.</p>	<p>The US Shareholder:</p> <ul style="list-style-type: none"> – must annually include in gross income as ordinary income its pro rata share of the ordinary earnings of the QEF and as long-term capital gain its pro rata share of the net capital gain of the QEF; – may elect to extend the time for payment of tax on its share of the undistributed earnings of the QEF until the QEF election is terminated; and 	<p>US investors</p>	<p>Non-US companies</p>

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		<ul style="list-style-type: none"> – maybe able to make a deemed sale election or a deemed dividend election, if the QEF election is not made within the first year of the US Shareholder's holding period in the PFIC. 		
Prohibited tax shelter transactions	<p>Generally prohibited tax shelter transactions are transactions which are:</p> <ul style="list-style-type: none"> – listed transactions (i.e. a transaction which is the same or substantially similar to one of the types of transaction that IRS has determined to be a tax avoidance transaction); – transactions with contractual protection (i.e. a transaction for which a party or related party has the right to a full refund or partial refund of fees if all or part of the intended tax consequences from the transaction are not sustained); or – confidential transactions (i.e. a transaction that is offered under the conditions of confidentiality and for which a party or a related party paid a minimum fee. A transaction is considered to be offered under conditions of confidentiality if the advisor places a limitation on your disclosure of the tax treatment or tax structure of the transaction and the limitation on disclosure protects the confidentiality of the advisor's tax strategies). 	US tax exempt investors will be subject to tax in relation to the income attributable to such transaction for the tax year in which the transaction took place, as well as subsequent tax year. In addition, there will be additional tax filing obligations for US tax exempt investors.	US tax exempt investors	Prohibited tax shelter transactions
Controlled foreign corporation ("CFC")	<p>A CFC is any non-US corporation in which:</p> <ul style="list-style-type: none"> – more than 50% of the voting rights; or – more than 50% of the total value of the stock, is owned directly, indirectly or constructively by US shareholders. 	US investors will have to report the income from the CFC and will be subject to tax on that income.	US investors	Non-US investments
Foreign Account Tax Compliance Act ("FATCA")	FATCA applies when non-US financial institutions and certain other non-financial non-US entities have US customers who hold non-US assets.	FATCA requires non-US financial institutions and certain other non-financial non-US entities to report on the non-US assets held by their US account holders or be subject to 30% withholding tax.	US investors	Non-US investments

Tax concepts

Form	Definition	Relevant investors	Relevant investments
Schedule K-1 form	The Schedule K-1 is a document issued for an investment in partnership interests. The purpose of the Schedule K-1 is to report a US investor's share of the partnership's income, deductions and credits.	US investors	US and non-US investments
W8 form	Non-US residents that earn income from one or more US sources fill in W8 forms in order to apply for an exemption from specified US information return reporting and withholding tax.	Non-US investors	US investments
W9 form	US-residents fill in W9 form in order to certify that the tax identification number is correct.	US investors	US and non-US investments

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