

**The Florida Senate**  
**BILL ANALYSIS AND FISCAL IMPACT STATEMENT**

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

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Prepared By: The Professional Staff of the Judiciary Committee

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BILL: SM 1344  
INTRODUCER: Senator Flores  
SUBJECT: U.S. Treasury/Deposits by Nonresident Aliens  
DATE: March 25, 2011      REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Arzillo</u>	<u>Burgess</u>	<u>BI</u>	<b>Favorable</b>
2.	<u>Boland</u>	<u>Maclure</u>	<u>JU</u>	<b>Favorable</b>
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

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**I. Summary:**

The memorial urges the United States Congress to direct the Department of Treasury to withdraw a proposed Internal Revenue Service (IRS) regulation that would require banks to report to the IRS all interest paid on deposit accounts held by any nonresident alien. Current IRS regulations only require that financial institutions report the interest paid on deposit accounts held by U.S. and Canadian citizens. Further, the memorial urges the United States Congress to hold hearings to examine the possible negative economic effects and costs of the proposed regulation on the United States, Florida, and financial institutions.

Copies of the memorial are to be provided to the President of the United States, the President of the United States Senate, the Speaker of the United States House of Representatives, and each member of the Florida delegation to the United States Congress.

**II. Present Situation:**

**Current Federal Regulation of Nonresident Alien Deposits**

Regulation 26 C.F.R. s. 1.6049-4 governs the authority of the Internal Revenue Service (IRS) to obtain reports of interest earned on bank deposits. Currently, the only nonresident aliens<sup>1</sup> subject to reporting interest earned on deposit accounts held in the United States are Canadians.<sup>2</sup> The

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<sup>1</sup> The IRS defines a nonresident alien as “an individual who is not a U.S. citizen or a resident alien. A resident of a foreign country under the residence article of an income tax treaty is a nonresident alien individual for purposes of withholding.” <http://www.irs.gov/businesses/small/international/article/0,,id=102319,00.html> (last visited Mar. 25, 2011).

<sup>2</sup> See 26 C.F.R. s. 1.6049-8(a) (“[I]nterest means interest paid to a Canadian nonresident alien individual . . . with respect to a deposit maintained at an office within the United States.”).

report requires the U.S. financial institution disbursing the interest earned on the deposit account to submit a 1042-S form, “Foreign Person’s U.S. Source Income Subject to Withholding,” each year interest is paid.<sup>3</sup> When a 1042-S form is submitted to the IRS, the financial institution is required to send a copy to the Canadian account holder giving notice that the form has been submitted to the IRS.<sup>4</sup> The interest paid to a Canadian nonresident alien is not subject to tax under 26 C.F.R. s. 3406.<sup>5</sup>

In 2002, the IRS attempted to broaden the nonresident alien depositors subject to the reporting requirement to 15 countries.<sup>6</sup> The 2002 proposed regulation also allowed for the reporting of all nonresident alien interest earnings, regardless of country of origin, if the financial institution desired.<sup>7</sup> This change in the regulations met with considerable opposition. A study estimated that \$88 billion would be removed from U.S. financial institutions upon the approval of this regulation.<sup>8</sup> Ultimately, the IRS did not make any changes to the regulation.

### **Proposed Changes to Regulation of Nonresident Alien Deposits**

In February of 2011, the IRS proposed a new set of changes to the regulations, which would withdraw the 2002 regulation. The 2011 proposed regulation would apply to interest earned on deposit accounts held by citizens of any foreign country. Therefore, financial institutions in all 50 states would be required to report all the interest earned on deposit accounts, \$10 or more, to the IRS using the 1042-S form, effective December 31 of the year of enactment.<sup>9</sup> Inasmuch as financial institutions are already required to report this information for deposit accounts held by U.S. and Canadian citizens, the same requirements for reporting to the IRS would be applied to deposit accounts held by all nonresident aliens, regardless of country of origin.<sup>10</sup> Additionally the proposed regulation would require the financial institution to furnish (either in person or by sending it to the person’s last known address) a copy of the 1042-S form to the recipient for interest paid on deposits maintained at a bank’s office within the United States.<sup>11</sup>

The IRS states several reasons for the regulatory change. First, the IRS states that there is a growing consensus among foreign countries to cooperate in information sharing for taxation purposes, including entering into agreements. The IRS believes that the proposed regulation signals to other countries that the United States will not withhold this tax information through

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<sup>3</sup> See 26 C.F.R. s. 1.6049-4(b)(5).

<sup>4</sup> See 26 C.F.R. s. 1.6-49-6(e)(4).

<sup>5</sup> See 26 C.F.R. s. 31.3406(g)-1(d) (“A payment of interest made to a Canadian nonresident alien individual under section 1.6049-8(a) of this chapter is not subject to withholding under section 3406.”)

<sup>6</sup>The countries subject to the 2002 proposed regulation were Australia, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, and the United Kingdom. KPMG Tax News Flash, *Proposed Regulations on Reporting of Deposit Interest Paid to Nonresident Aliens; Prior Proposed Regulations Are Withdrawn—Again*, January 6, 2011, TaxNewsFlash No. 2011-12, <http://www.us.kpmg.com/microsite/taxnewsflash/2011/Jan/1112.html>.

<sup>7</sup> *Id.*

<sup>8</sup> Kenric Ward, *Florida Bankers Assail IRS Reporting Rule for Nonresident Aliens*, <http://sunshinestatenews.com/blog/florida-bankers-assail-irs-reporting-rule-nonresident-aliens> (last visited Mar. 24, 2011).

<sup>9</sup> See Internal Revenue Bulletin: 2011-8, REG-146097-09, *Notice of Proposed Rulemaking; Notice of Public Hearing; and Withdrawal of Previously Proposed Rulemaking Guidance on Reporting Interest Paid to Nonresident Aliens*, [http://www.irs.gov/irb/2011-08\\_IRB/ar13.html](http://www.irs.gov/irb/2011-08_IRB/ar13.html) (last visited Mar. 24, 2011).

<sup>10</sup> *Id.*

<sup>11</sup> *Id.*

bank secrecy, or due to a lack of taxable incentives. Also, the IRS states that the new regulations will strengthen the United States exchange of information program, and the IRS believes that the new requirement will limit U.S. taxpayer evasion of taxes. Presently, such evasion could occur if a U.S. citizen makes a false claim of foreign status when establishing such a deposit account.<sup>12</sup>

These changes have been met with strong opposition. Congressman Bill Posey (Fla. 15th) has collected the signatures of the entire Florida delegation of U.S. Congressmen on a letter stating that the delegation is opposed to the change in the regulatory scheme. One principal concern expressed in the letter is the loss of foreign deposits. The letter states that the proposed regulation may lead to an exodus of nonresident alien depositors that could amount to the loss of hundreds of billions of dollars in foreign deposits for financial institutions.<sup>13</sup> Additionally, the letter points out that the withdrawal of funds by multiple investors at once might affect the solvency of financial institutions that rely heavily on these nonresident alien depositors.<sup>14</sup> Finally, the letter cites an explicit congressional intent to attract and retain capital in the U.S. economy and states that the United States' competitive advantage will be weakened because nonresident aliens are likely to remove their deposits from U.S. financial institutions and will redeposit those monies in foreign financial institutions.<sup>15</sup>

### III. Effect of Proposed Changes:

Whereas current Internal Revenue Service (IRS) regulations only require that financial institutions report the interest paid on deposit accounts held by U.S. and Canadian citizens, recently proposed regulations would require that financial institutions report, to the IRS, interest paid on deposit accounts held by a citizen of any country. This memorial urges the United States Congress to direct the Department of Treasury to withdraw proposed IRS regulation REG-146097-09, and to hold hearings to examine the possible negative effects and costs of the proposed regulation on the United States, Florida, and financial institutions. The memorial provides that it will be sent to the President of the United States, the President of the U.S. Senate, the Speaker of the U.S. House of Representatives, and to each member of the Florida delegation to the U.S. Congress. The memorial's "whereas" clauses assert that:

- Florida is the "Gateway to the Americas," and has promoted international trade and finance;
- The United States has a longstanding policy of encouraging nonresident aliens to deposit their funds in U.S. financial institutions, which fosters economic development in the United States and Florida;
- Federal law does not permit taxation of nonresident alien deposits;
- Nonresident aliens have deposited nearly \$3 trillion in banks and with securities brokers in the United States;
- Nonresident aliens have deposited tens of billions of dollars in financial institutions in Florida;
- Many of the nonresident aliens who have deposited funds in Florida financial institutions are Latin Americans who do not trust the privacy of the institutions in their home countries, and

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<sup>12</sup> *Id.*

<sup>13</sup> Letter sent to President Obama from the Florida Delegation in Washington, D.C., March 2, 2011, *available at* <http://posey.house.gov/UploadedFiles/IRS-DelegationLetter-March3-2011.pdf> (last visited Mar. 24, 2011).

<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

fear kidnapping, extortion, and financial instability when their funds are domestically deposited;

- The proposed Treasury rule would place U.S. and Florida financial institutions at a competitive disadvantage; and
- Removal of nonresident alien deposits would drive job-creating capital out of Florida.

**IV. Constitutional Issues:**

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

**V. Fiscal Impact Statement:**

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

None.

C. Government Sector Impact:

None.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

**VIII. Additional Information:**

A. Committee Substitute – Statement of Substantial Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.

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This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.

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