DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
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Dear :

This letter responds to your request for information dated March 5, 2008. In your letter, you requested certain information about the tax treatment of a lump-sum distribution from a qualified U.K. pension scheme paid to a U.S. resident.

Under the Internal Revenue Code, the United States generally taxes its residents on their worldwide income, regardless of their citizenship or the source of their income. However, an income tax treaty to which the United States is a party could change the application of the law. The United States has an income tax treaty with the United Kingdom (the Treaty).

Article 17(1) of the Treaty provides that:

> a) Pensions and other similar remuneration beneficially owned by a resident of a Contracting State shall be taxable only in that State.
>
> b) Notwithstanding sub-paragraph a) of this paragraph, the amount of any such pension or remuneration paid from a pension scheme established in the other Contracting State that would be exempt from taxation in that other State if the beneficial owner were a resident thereof shall be exempt from taxation in the first-mentioned State.

Article 17(2) of the Treaty provides that:

> Notwithstanding the provisions of paragraph 1 of this Article, a lump-sum payment derived from a pension scheme established in a Contracting State and beneficially owned by a resident of the other Contracting State shall be taxable only in the first-mentioned State.

Although Article 17(2) provides that the Contracting State in which the pension scheme is established has the exclusive right to tax a lump-sum payment, Article 1(4) of the Treaty contains a “saving clause” that allows the United States to tax its residents and citizens as if the Treaty had not come into effect.

Article 1(4) of the Treaty provides that:

> Notwithstanding any provision of this Convention except paragraph 5 of this Article, a Contracting State may tax its residents (as determined under Article 4 (Residence)), and by reason of citizenship may tax its citizens, as if this Convention had not come into effect.

Article 1(5) of the Treaty provides a number of exceptions to the saving clause, but there is no exception for Article 17(2). Therefore, the saving clause overrides Article 17(2) and allows the United States to tax a lump-sum payment received by a U.S. resident from a U.K. pension plan.

This letter has called your attention to certain general principles of the law. It is intended for informational purposes only and does not constitute a ruling. <u>See</u> Rev. Proc. 2008-1, §2.04, 2008-1 IRB 7 (Jan. 7, 2008).

If you have any additional questions, please contact at
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Sincerely,

M Grace Fleeman
Senior Technical Reviewer, Branch 1
(International)