Recommendation No. 30:

Eliminate (with respect to income not connected with the conduct of a trade or business) the provisions for progressive taxation of U.S. source income of nonresident alien individuals in excess of $19,000 and provide that no nonresident alien whose tax liability is fully satisfied by withholding shall be required to file returns.

The provision for progressive taxation of foreign investors and the companion requirement to file returns, in our opinion constitutes one of the major sources of confusion and misunderstanding for potential foreign investors in the United States. The revenues produced by this tax are understood to be negligible. Progressive taxation of foreign investors does not exist in many other industrialized countries of the world.

Treaties with most industrialized countries already eliminate the provision for progressive taxation of nonresident alien individuals who are residents of treaty countries. However, there are throughout the world vast sums of capital that have left their countries of origin. Typically, these funds are held in treaty countries by residents of nontreaty countries. If the provisions for progressive taxation of nonresident alien individuals were removed from the Code, the position of the United States in competing with other industrialized nations for such capital would be strengthened.

Furthermore, we must recognize that the actual fiscal impact of this, or any other, tax law on the persons to whom it applies does not measure the extent to which the law deters or limits potential investment by persons who are unwilling or unable to master its complexities. This is especially true when dealing with foreigners, whose familiarity with U.S. laws and practices is limited. Even those foreigners with substantial funds available for investment often find it troublesome and expensive to obtain sound U.S. tax advice, with the result that they channel their investments elsewhere.

Were the Internal Revenue Code amended to eliminate progressive taxation of nonresident alien individuals not engaged in trade or business within the United States, the entire U.S. tax liability of substantially all such aliens would automatically be fully satisfied by withholding at the source. These aliens would have no actual, or potential, additional tax liability and no returns