

42 REMOVE TAX BARRIERS TO FOREIGN INVESTMENT IN U.S.

The questions involved in this recommendation are not generally covered by existing treaties. Treaties are concerned with a question of "a permanent establishment" and not the definition of a trade or business.

4. *Real property income and mineral royalties*

The Treasury recommends that nonresident alien individuals and foreign corporations be given an election to compute income from real property and mineral royalties on a net income basis and be taxed at graduated rates on such income as if engaged in a trade or business in the United States. The Fowler task force made no comparable recommendation.

Under existing treaties nonresident alien individuals from many countries can now elect to be subject at regular tax rates on a net basis by filing form 1040-B. The countries involved are Australia, Austria, Belgium, Finland, France, Germany, Greece, Honduras, Ireland, Italy, Japan, Netherlands, Netherlands Antilles, Norway, South African, Switzerland, United Kingdom, and United Kingdom colonies. In addition, Canadian nonresident aliens can elect such treatment by filing form 1040-B but only on real property income.

5. *Capital gains*

The Treasury proposes to eliminate the provision taxing capital gains realized by a nonresident alien when he is physically present in the United States, and to extend from 90 to 183 days the period of presence in the United States during the year which makes nonresident aliens taxable on all their capital gains. The Fowler task force made a similar recommendation, but instead of the figure 183 days used 180 days.

Our treaties with Canada, France, Sweden, and the United Kingdom exempt to some extent capital gains derived by residents of those countries having no permanent establishment in the United States. The United Kingdom and Canadian treaties exempt all capital gains; the Swedish treaty exempts all capital gains except those derived from transfers of real property; and the French treaty exempts only capital gains from transfers of securities.

6. *Personal holding company and "second dividend" taxes*

The Treasury proposal is identical with the Fowler task force recommendation in exempting foreign corporations owned entirely by nonresident alien individuals, whether or not doing business in the United States, from the personal holding company tax. In addition, the Treasury proposes to nullify the application of the "second dividend" tax of section 861(a)(2)(B) so that it only applies to the dividends of foreign corporations doing business in the United States which have over 80 percent U.S. source income.

7. *Estate tax exemption and rates*

The Fowler task force recommended eliminating U.S. estate taxes on all intangible personal property of nonresident alien decedents. The Treasury did not act on this recommendation but instead proposes to increase the \$2,000 exemption from tax to \$30,000 and substitute for regular U.S. estate tax rates (which go as high as 77 percent) a 5-10-15 percent rate schedule.

Under the applicable treaties, debt obligations normally have their situs either in the domicile of the decedent or at his place of residence. However, stocks normally have their situs at the place of incorporation under the treaties. Presumably the stock of U.S. corporations is included in many of the estates of nonresident aliens and the Fowler task force recommendation would have had an impact in these cases.

The proposal of the Treasury to increase the \$2,000 exemption to \$30,000 will provide benefits to the estates of nonresident aliens where the applicable treaties govern, because of the type of exemption usually provided in the treaties. Under the usual exemption, a contracting state in imposing taxes on a decedent not domiciled at the time of his death in its territory must grant a portion of its specific exemption to the estate. Subject to certain variations, the portion of the exemption granted bears the same proportion to the total exemption as the property taxed bears to the total estate of the decedent. By raising the specific exemption the U.S. raises the dollar amount of the exemption that will normally be granted to a nonresident alien's estate. This type of exemption is granted in the estate tax treaties with Australia, Finland, France, Greece, Italy, Japan, Norway, and Switzerland. The Canadian treaty contains a different exemption which will also be liberalized by the Treasury's proposal.