

However, another of the obstacles to the inclusion of foreign banks and firms in such underwriting groups lies in the tax field. Rather than eliminating this obstacle, the current provision of H.R. 5916 would make it more acute.

In many underwriting groups the syndicate manager reserves the right to sell certain of the securities being underwritten to institutions and dealers on behalf of the members of the syndicate, to engage in stabilizing transactions, and to take certain other actions which may result in the realization of a profit by all members of the group. There is considerable risk that in taking such actions the syndicate manager may be regarded as the agent of all of the other members of the group.

Under section 3 of the bill the definition of "engaged in trade or business within the United States" appearing in IRC section 871(c) would be amended to provide that nonresident alien investors who are not dealers in securities or commodities could grant discretionary authority to a U.S. agent or broker without thereby being deemed to be engaged in trade or business within the United States.

The clear implication of this provision in its current form is that a dealer in securities or commodities will be deemed to be engaged in trade or business in the United States if any discretion is granted to a U.S. agent. Thus, the risks to a foreign bank or securities firm of participating in a U.S.-managed underwriting group would become acute.

The current text of these proposals raises certain other problems. Under the proposed amendments, any foreign bank,¹ securities firm or commodities firm granting discretionary power to a U.S. agent or securities or commodities broker would be regarded as engaged in trade or business here. This would be true even if the discretionary authority was in fact granted on behalf of individual or corporate clients of the foreign bank or firm, or if the discretionary authority was granted with respect to the investment account of the bank or firm.

In view of the fact that a very substantial portion of the securities and commodities business received from nonresident alien individuals and foreign corporations is effected through foreign banks and dealers, it appears that the current text of the proposals would, in many cases, fail to have the intended effect and might, in fact, have an adverse effect on our balance of payments.

As is recognized in the Treasury press release accompanying H.R. 5916, the granting of a discretionary power of investment "does not really bear a relation to the foreigner's ability to carry out transactions in the United States—the discretionary power is merely a more efficient method of operating rather than having the investor consulted on every investment decision and frequently is merely a safeguard to protect him in case of world turmoil."

The above considerations appear applicable in cases where a foreign bank or securities firm is operating its own investment account or acting on behalf of its customers as well as in cases of a direct grant of authority from a nonresident alien individual to a U.S. broker.

While it is equitable that a foreign bank or firm should not be permitted to operate a regular business in the United States as a securities or commodities dealer without being deemed to be engaged in trade or business here, the bill could be amended to take care of this situation without creating the problems referred to above.

It is suggested that the proposed amendments to IRC section 871(c)(2) be altered to read as follows:

"(2) TRADING IN SECURITIES OR COMMODITIES.—

(A) SECURITIES.—Trading in stock or securities whether transactions are effected directly, or by way of an agent, through a resident broker, commission agent, custodian, or other independent agent, and (except where such stocks or securities are held by the taxpayer primarily for sale to customers in the United States in the ordinary course of its trade or business) whether or not any such agent has discretionary authority to make decisions in effecting such transactions, or

(B) COMMODITIES.—Trading in commodities whether transactions are effected directly, or by way of agent, through a resident broker, commission agent, custodian, or other independent agent, and (except where such commodities are held by the taxpayer primarily for sale to customers in the United States in the ordinary course of its trade or business) whether or not any such agent has discretionary authority to make decisions in effecting such transactions, if such commodities are of a kind customarily dealt in on an organized commodity exchange and if the transaction is of a kind customarily consummated at such place."

¹ Contrary to U.S. practice most foreign banks are "dealers" in securities.