

In addition, it should be made clear by regulation or published ruling that a foreign dealer or underwriter would not be deemed to be engaged in trade or business hereby reason of participation in an underwriting group having a U.S. manager.

2. *Taxation of securities profits of resident foreign corporations*

Under section 4 of the bill a resident foreign corporation would be taxed at ordinary rates on its business income from U.S. sources and at a flat 30-percent rate on its nonbusiness income from U.S. sources.

Business income and nonbusiness income are defined as follows in the proposed amendments to IRC section 882:

"(3) BUSINESS INCOME DEFINED.—In the case of a foreign corporation business income includes all income derived from sources within the United States other than the income described in paragraph (4), except that business income shall not include gain from the sale or exchange of stock in a corporation.

"(4) NONBUSINESS INCOME DEFINED.—In the case of a foreign corporation nonbusiness income shall consist of dividends and amounts described in section 631 (b) and (c) which are considered to be gains from the sale or exchange of capital assets."

Under these definitions gains realized by a foreign corporation from the sale of corporate stock would be excluded from both business and nonbusiness income and, therefore, totally exempt from U.S. tax.

In most cases this exclusion will serve the basic purpose of H.R. 5916. However, under the bill as currently drafted, it would be possible for U.S. persons to finance and operate a securities dealer business in the United States through the medium of a resident foreign corporation and thereby accumulate profits from trading in corporate stock substantially free of tax at the corporate level.

If the corporation were a "regular dealer in stock or securities," its income from sales of corporate stock would not be "foreign personal holding company income" or "Subpart F income" and the shareholders would be subject to tax only on amounts actually distributed to them by the corporation (see IRC secs. 543(a)(2), 952, 954). Therefore, a substantial tax benefit might be accorded to persons making no contribution to an improvement of the U.S. balance of payments.

This apparently unintended result could be eliminated by amending the definition of business income to read as follows:

"(3) BUSINESS INCOME DEFINED.—In the case of a foreign corporation business income includes all income derived from sources within the United States other than income described in paragraph (4), except that business income shall include net gains from the sale or exchange of stock in corporations only if such stock is held by the taxpayer primarily for sale to customers in the ordinary course of its trade or business."

Mr. ULLMAN. We have two additional witnesses.

Unfortunately, we have to adjourn for the day. Mr. Anderson, will it be possible for you to come back tomorrow?

Mr. ANDERSON. Yes, sir.

Mr. ULLMAN. Tomorrow morning at 10 o'clock. And Mr. Waris?

Mr. WARIS. Yes.

Mr. ULLMAN. We will expect you back here then in this committee room at 10 a.m., and the committee is adjourned until 10 o'clock tomorrow morning.

(Whereupon, at 12:47 p.m., the committee recessed to reconvene at 10 a.m., Thursday, July 1, 1965.)