

substantial active businesses here through branches. Foreign banks are one example of the type of foreign corporation that would be adversely affected by the proposed amendment.

Generally, banks in their foreign operations prefer to conduct business through a branch, rather than through a subsidiary, in order to have the benefit of their "home office" reserves or deposits. In New York alone, there are about a dozen foreign banks that conduct operations through branch offices. A number of such banks have wholly owned domestic subsidiaries which engage in businesses that the parent is not permitted to engage in directly. Thus, a number of foreign banks have wholly owned domestic subsidiaries that conduct a fiduciary business or a safe deposit business.

There are undoubtedly a number of other legitimate business reasons which require foreign corporations to conduct their business operations in the United States in branch form rather than through domestic subsidiaries. For example, a foreign corporation might not be permitted to assign certain assets (such as a license, franchise, or trademark) needed in the conduct of a particular business in this country. Or it may be that charter provisions or debt restrictions prevent a foreign corporation from transferring assets to a U.S. subsidiary or from conducting particular activities through a U.S. subsidiary.

Aside from the banking fields, there are other areas where the proposed amendment would work undue hardship. At least one of the large Japanese trading companies has several branch offices in the United States. These branch offices generate annual sales of between \$300 and \$400 million. This Japanese trading company has also acquired a majority stock interest in at least one U.S. operating subsidiary. Perhaps the widest use by foreign corporations of branch offices, together with affiliated domestic subsidiaries, as a means of conducting business in this country occurs in the insurance field. It is interesting to note that foreign insurance companies which conduct an insurance business here through branch offices are not affected by the proposed amendment. The reason that their right to the intercorporate dividend deduction was not disturbed is probably because of the Treasury's recognition of the wide use made of this type of operation in the insurance industry. (It is likely, however, that there are situations where foreign insurance companies do, through branch operations, engage in other types of business in this country, such as the management of domestic subsidiaries which conduct an insurance or other business. Such foreign insurance companies would be adversely affected by the proposed amendment.)

The issue certainly is not a hypothetical matter, for the above-described situations represent specific, concrete examples of foreign corporations which conduct business here in branch form and which would be hurt by the proposed amendment although they do not fit within the specific rationale underlying the amendment. To deprive foreign corporations, which conduct business through this type of structure, of the intercorporate dividends received deduction would cause severe dislocation of legitimate, long-standing business operations in this country by foreign corporations.

C. The effect of the proposed amendment might also be to discourage existing and potential investment in this country by foreign corporations with branch offices here

Although the amendments to sections 881 and 882 proposed by the Treasury would in general appear to stimulate investment in U.S. securities (especially by foreign individuals and probably to a lesser extent by foreign corporations) as a result of the elimination of any tax on capital gain realized upon U.S. stock investments,¹ the amendment might very well have the additional effect of discouraging existing and potential long-term investment in this country by a number of large foreign corporations which conduct substantial, active businesses here through branch operations and through domestic subsidiaries. This result appears unwarranted and unintended in view of the fact that (1) the manifest purpose of H.R. 5916 is to stimulate foreign investment in the United States and (2) this type of operation involves no abuse or element of tax avoidance.

III. RECOMMENDATIONS

It is our belief that dividends received by foreign corporations from U.S. subsidiaries in which they have made significant and permanent-type investments

¹ It is a well-known fact that the yield on U.S. stocks is generally lower than on foreign stocks, but that the appreciation factor on U.S. stocks is often attractive to foreign investors.