

more often than not, is specifically excluded from the concept of "income from real property." It is therefore recommended that proposed section 871(d)(A) be amended to make it clear that interest from mortgages on real property is not "income from real property." A similar change should be made in proposed section 882(d).

Proposed sections 873(a) and 882(c)(1)(A), in providing for the allowance of deductions and credits in respect of U.S. income, limit the deductions to circumstances in which they are "effectively connected with the conduct of a trade or business within the United States." It is recommended that these proposed sections be changed by inserting "attributable to income which is" immediately preceding the phrase quoted in the preceding sentence, so that it is clear when an election is made to treat real property income as income connected with a U.S. business that such election effectively permits the non-resident to obtain the offsetting deductions, the purpose of the election in the first instance.

Finally, the committee questions whether the election under sections 871(d) and 882(d) should extend to gains described in present code section 631(b) or (c). Since such gains are also defined as periodic income, it would appear that a nonresident individual or corporation would always make the election in order to obtain a lower effective tax rate and possible use of such deductions against other business income.

Foreign corporations

Under section 4, a foreign corporation engaged in trade or business in the United States, like a nonresident alien similarly so engaged, would be taxed as if it were a resident on its taxable income which is effectively connected with the trade or business conducted here. Again, it appears that the concept of "effectively connected with the trade or business" is intended to be broader than the present concept of gross income from U.S. sources. For the reasons stated in the discussion of section 2 of the bill, it is believed that this change is inadvisable.

Section 4(a). Tax on income not connected with U.S. business

The title suggested for proposed code section 881, "Income of Foreign Corporations Not Connected With U.S. Business," fails to indicate, as it should, that a tax is imposed by that section. Accordingly, it is recommended that the section's title be amended by the addition of "Tax on" at the beginning thereof.

Proposed section 881(a)(1), reflecting changes made in proposed section 861(a)(1)(A), would eliminate from the category of non-taxable interest, interest on deposits with persons carrying on the banking business. For the reasons stated in the discussion of section 2(a) of the bill, it is believed that this change is inconsistent with the purpose of the bill to encourage foreigners to invest in the United States.

Proposed section 881(a) also would expand the definition of periodic income from U.S. sources (income subject to 30 percent tax) to include income from the sale or liquidation of a collapsible corporation (sec. 341) and from original issue discount (sec. 1232). For reasons stated in the discussion of section 3 of the bill, it is believed this extension of the definition of "periodic income" is inadvisable.