

items of pseudo capital gain already taxed to nonresident alien individuals and foreign corporations as investment income would be. However, lumping these two classes of income with investment income produces technical problems which the bill does not resolve. Moreover, this treatment appears to overlook policy problems which are interlocked with the technical problems.

#### TECHNICAL PROBLEMS OF ENFORCEMENT

The bill would amend section 1441(b) to revise the definition of items subject to withholding, but would not require withholding out of section 341 or section 1232 gains which would be taxed by the amended sections 871 and 881. Therefore, as the bill stands, there seems little prospect that the law taxing these gains would be enforced effectively. At the same time, it must be conceded that to require withholding from section 1232 gains would be cumbersome and to require withholding from section 341 gains would not only be burdensome, but could result in serious and unjustified penalties on domestic taxpayers.

Withholding from section 1232 gains would be mechanically difficult in even the simplest case, since the section 1232 gains realized by various taxpayers who sell bonds of a single series on the same day will vary according to their holding periods. More important, section 1232 applies only when a creditor has, overall, realized a gain from a sale of a debt instrument or upon its retirement. Accordingly, a withholding agent would be unable to compute the section 1232 gain of a seller (or holder at maturity) even if he knew the creditor's holding period and the total original issue discount inherent in the debt instrument at its inception. The withholding agent would have to know the taxpayer's basis as well.

To apply the rules of section 1441(c) (5) to withholding on section 1232 gains would be an extremely harsh remedy, completely inconsistent with the basic purpose of the bill. A modified version of the rule of section 1441(c) (5) could be drawn to require that 30 percent of all the original issue discount inherent in a debt instrument (not 30 percent of the proceeds from its sale or retirement) be withheld unless the creditor provided the withholding agent with the data concerning his holding period and basis required to make the necessary computations.

Even a withholding tax based on the principle of section 1441(c) (5) could be avoided readily in most cases by foreign holder A selling a U.S. debt instrument originally issued at a discount to foreign holder B outside the United States. B would thereby be placed in a position in which he could present the instrument for payment or sell it in a U.S. market, with a full disclosure of all facts relevant to his ownership but avoid withholding almost completely because the section 1232 gain allocable to his ownership would be minute. There would seem to be no practical method of guarding against this. In particular, full withholding levied against the last foreign holder, leaving him to recoup against his assignors and his assignors' predecessors would often produce more tax than would be due from a series of domestic holders all taxable at 30 percent, since some of the remote holders may have been people who have realized overall losses from