

tively connected" income from foreign sources would not, it is felt, justify the proposed radical departure from the older rules. Moreover, the proposed extension does not fall within one of the stated objectives of the bill to encourage foreign investment in the United States.

*Bill section 3(a)(1): IRC section 871(a)(1)—Periodic income*

This section imposes a flat 30-percent tax on periodic income of nonresident aliens which is not effectively connected with the conduct of a trade or business within the United States. The familiar enumeration of interest, dividends, rents, etc. is retained. Also retained is the taxation of gains under section 1235 (gains from the sale or exchange of patents). In addition, the 30-percent tax will now apply to gain on the sale, exchange, or liquidation of stock of a collapsible corporation (sec. 341) and to "interest" earned on bonds or other original discount debt instruments issued after a specified date (sec. 1232).

The provisions of new proposed section 871(a)(2) (relating to capital gains) will not apply to section 1235 income. It therefore appears that capital losses cannot offset section 1235 gains. In effect, gains realized by nonresident alien inventors would be treated as ordinary investment income, subject to a 30-percent tax, without offset. The law thus discriminates against foreign inventors, as it denies them the capital gain treatment accorded resident inventors, with the anomalous result that a relief statute (sec. 1235) actually results in a detriment to a foreign inventor who might, but for section 1235, get capital gain treatment under sections 1221 *et seq.* Consideration should be given to allowing foreign inventors capital gain treatment (often resulting in no tax) to the extent that they would qualify therefor without the benefit of section 1235.

*Bill section 3(a)(1): IRC section 871(a)(2)—Capital gains*

This section imposes a capital gains tax upon nonresident alien individuals who are present in the United States for 183 days or more during the taxable year at the flat rate of 30 percent. No capital gains tax is imposed upon foreign corporations except to the extent that such gains are effectively connected with a U.S. trade or business. Sections 881, 882.

A question exists as to the proper tax treatment of sales made on the installment basis. If a nonresident alien is present for the required period during the year of sale but is not present in the United States for the required period during the year of receipt of an installment, it would appear that he is not subject to tax under section 871(a)(2) in respect of such installment.

It is to be noted that no provision is made in respect of the capital gains of foreign estates or trusts. Since in many cases it is difficult to conceive of a "presence" in the United States of a foreign estate or trust, except inventories, it would appear that such estates or trusts may often not be subject to U.S. tax on its capital gains.

Although the subcommittee prefers not to comment on policy questions, the members of the subcommittee believe that the proposed capital gains tax on nonresident aliens would not only be difficult to enforce but is in the nature of a "nuisance" tax rather than a revenue