

United States is something which should be approached cautiously because of the possibility of inadvertently becoming subject to tax.

The Internal Revenue Code now provides for a general exemption from capital gains tax for nonresident foreigners not doing business in the United States with two exceptions. First, the foreigner's gains are subject to U.S. capital gains tax if he is physically present in the United States when the gain is realized, and second, all gains during the year are taxable if he spends 90 days or more in the United States during that year.

The physical presence restriction can be easily avoided by the experienced foreign investor if he arranges to be outside the country when the gain is realized, but is a potential trap to the foreigner who is not aware of its existence. The bill would eliminate this restriction from the general capital gains exemption.

In addition, the bill would extend the 90-day period which a foreigner may spend here without being subject to capital gains tax to 183 days. This will make the provision more consistent with international standards governing the taxation of foreigners residing in a country for a substantial period. It will also minimize a foreigner's fear that he will be taxed on capital gains realized at the beginning of a taxable year if he later spends a substantial amount of time in the United States during that year.

Graduated income tax rates.—At the present time, foreign individuals not doing business in the United States who derive more than \$21,200 of investment income from U.S. sources are subject to regular U.S. income tax graduated rates on that income and are required to file returns. (Below that figure a flat 30-percent rate applies.) These requirements have produced little revenue, in part because we have eliminated graduated rate taxation of investment income in almost all of our treaties with the other industrialized countries and in part because of the relative ease with which this provision is avoided. However, the possibility of being subjected to graduated rate taxation and the accompanying return requirement may be a source of concern to foreigners and consequently act as a substantial deterrent to foreign investment in the United States.

H.R. 13103 eliminates this form of taxation of nonresident foreigners not doing business here and removes the requirement for filing returns in such cases. The liability of foreign investors deriving U.S. investment income would thus be limited to the tax withheld at the statutory 30-percent rate or a lower applicable treaty rate. The legislation would continue graduated rate taxation for foreigners who are doing business in the United States. These rules are consistent with the practices of most other industrialized countries.

Definition of "engaged in trade or business".—H.R. 13103 makes clear that nonresident alien individuals or foreign corporations are not engaged in trade or business in the United States—and thus are subject to tax at the 30 percent withholding rate or lower treaty rate rather than at regular graduated rates—because of investment activities here or because they have granted a discretionary investment power to a U.S. banker, broker or adviser. This provision should have the effect of removing much of the uncertainty which now surrounds the question of what amounts to engaging in trade or business in the United States. Uncertainty of this type is undesirable as a matter of