

it earns anywhere in the world *outside* the United States, if such income is "effectively connected" with business activities by it in the United States.

Although H.R. 13103 has substantially modified and restricted the application of this "effectively connected" theory, it still pervades the Bill, the phrase being repeated scores of times throughout the first 63 of its 82 pages. The exact meaning of this phrase defies definition.

It is so vague that it would cause endless uncertainty, confusion and disputes. This is one point on which all who have examined this Bill and its predecessor agree. We believe that no amount of "legislative history" could adequately cure this defect.

One of the serious defects in this respect is that H.R. 13103 apparently would tax *all* of any item of income earned abroad which was "effectively connected" with certain United States activities of a foreign corporation, without regard to the *extent* that such income was "attributable" to those activities.

This is contrary to the intention clearly expressed in the House Ways & Means Committee report, to limit the application of the "effectively connected" theory so as to tax only so much of the foreign earned income as is attributable to activities in the United States. (p. 16) However, in its present form, H.R. 13103 makes no provision for any allocation, but would levy the tax on an "all-or-nothing basis. This will be confirmed in statements filed by others with your Committee.

4. *Recommended limitation of application of the "effectively connected" theory so as to exclude U.S. controlled corporations*

In order for this Bill to afford U.S. tax incentives to foreign investment in this country, application of the radical new "effectively connected" theory to U.S. owned and controlled corporations is not necessary; would be harmful; and should be eliminated.

This could be accomplished by substituting for the presently proposed new IRC Sec. 882(b) the following:

"SEC. 882. INCOME OF FOREIGN CORPORATIONS CONNECTED WITH UNITED STATES BUSINESS.—

* * * * *

(b) GROSS INCOME.—

1. In the case of foreign corporation 50 percent or more of the stock of which is owned, directly or indirectly, by United States persons (as defined in Section 957(d)), gross income includes only gross income from sources within the United States and,

2. In the case of all other foreign corporations, gross income also shall include gross income from sources without the United States which is effectively connected with the conduct of a trade or business within the United States.

The foregoing proposed provision would take away from foreign investor-owned foreign corporations no benefits which they would be able to obtain under the present provisions of H.R. 13103.

Another, simpler method to accomplish exactly the same purpose, with fewer changes in wording and cross-references, would be to reword the proposed new Sec. 864(c) (4) (C) (page 16 of the Bill as introduced) as follows:

"(C) No income, gain, or loss from sources without the United States shall be treated as effectively connected with the conduct of a trade or business within the United States if it either—(i) is derived by a foreign corporation, more than 50% owned, directly or indirectly, by U.S. persons, or (ii) is subpart F income within the meaning of section 952(a)."

5. *No revenue considerations to bar elimination of the "effectively connected" provisions of H.R. 13103*

The Ways & Means Committee report on H.R. 13103 (p. 7) shows that its "effectively connected" provisions would produce no tax revenue. Hence, the need for tax revenue can not be used as an argument against the elimination of this complicated source of uncertainty and endless disputes and difficulties, with all its undesirable features.

6. *Proposed disallowance of credit for uncertain foreign income taxes*

H.R. 13103 would disallow credit (or deduction) for foreign income taxes imposed on a foreign corporation if—

(1) Such taxes were imposed by reason of its place or organization or domicile, or