

I have prepared a more detailed statement which I have submitted to the clerk of the committee as I do not wish to burden the committee with a lengthy oral presentation.

Thank you. I have submitted a more detailed statement.
(The document referred to above follows:)

STATEMENT OF JOHN SEATH, VICE PRESIDENT AND DIRECTOR OF TAXES OF
INTERNATIONAL TELEPHONE & TELEGRAPH CORP.

Mr. Chairman and members of the Committee, my name is John Seath and I am Vice President and Director of Taxes of International Telephone and Telegraph Corporation.

You are holding hearings today on H.R. 13103, the Foreign Investors Tax Act of 1966, which is subtitled "A bill to provide equitable tax treatment for foreign investment in the United States." I am certain that from all the testimony you have heard and will hear on this bill, some doubts will be created whether the bill does, in fact, accomplish this objective.

The Treasury Department which strongly supports the bill has repeatedly stated that the bill is part of the President's program to improve the United States balance of payments. I am here to urge consideration by your Committee of an amendment which will, I submit, substantially encourage repatriation by domestic corporations of earnings of foreign subsidiaries and thereby directly improve our balance of payments situation.

As your Committee may well know, many U.S. corporations are already in difficulties because they have foreign tax credits currently unusable in part because of the interpretation of the present foreign tax credit provisions of the Internal Revenue Code. Understandably, these corporations are reluctant to withdraw from foreign subsidiaries further dividends which carry with them a high foreign tax liability not currently creditable in full against U.S. tax liability. This potential excess tax liability serves severely to inhibit dividend repatriation, and the U.S. balance of payments situation is thereby adversely affected.

I respectfully urge your Committee to consider an amendment to the bill which will eliminate this impediment to the withdrawal of dividends from foreign subsidiaries. Not only would such an amendment restore the foreign tax credit limitation to the interpretation followed by the Internal Revenue Service prior to two court decisions some twenty years old, but it would give substantial assistance to taxpayers seeking to support the economic policies of the United States. It is believed that any loss in revenue to the Treasury will be far outweighed by the increased flow of foreign earnings to the United States.

A basic principle of the foreign tax credit is that a taxpayer is allowed a credit against U.S. tax not to exceed the ratio that its foreign taxable income bears to its entire taxable income, both foreign and domestic. However, an unintended quirk in the interpretation of the tax law cuts down the maximum foreign tax credit allowable by reducing the numerator of the limiting ratio. This results because indirect expenses (expenses not allocable to a specific class of income) must be allocated to dividends received from foreign subsidiaries, even though no portion of the expenses is properly applicable to such dividend income. In spite of our treaty program, this leads to double taxation since the foreign country imposing the tax properly allows no deduction for such expenses. The effect of this rule is not limited to dividend income; it applies to all foreign income, but its most extreme application is against foreign dividend income.

As a result, many U.S. corporations, if they wish to repatriate earnings from their foreign subsidiaries, have to pay an aggregate U.S. and foreign tax liability substantially in excess of the tax paid on the same amount of income by corporations operating entirely in the United States. This can easily be illustrated by the following examples:

Assume a domestic corporation realizes gross income of \$150 from sources within the United States and \$100 from sources without the United States (either foreign royalties of \$100 on which \$48 of foreign taxes were paid, or dividends of \$52 from its foreign subsidiary which amount, after gross-up, is treated as \$100 of foreign dividend income since the subsidiary paid \$48 of foreign taxes with respect to the dividends). (It should be noted here that the gross-up provisions of the 1962 Revenue Act substantially increase the tax distortion caused by the present foreign tax credit computation rules.) Assume, further, that the foreign income was received without any expense and that the domestic corporation