

There is also a serious question whether the income taxed by the United States under this new provision would, under the bill, be limited to the portion fairly allocable to the services performed in the U.S. office.

Indeed, unless a section 482 type of allocation formula were added to the provision, this aspect of the provision might simply become a trap for the unwary, and for the small taxpayer, since it could perhaps be avoided in many cases by the formation of a separate subsidiary to conduct the activities of the U.S. office.

Serious policy questions are also presented by the fact that the new provision is in direct conflict with most of the present U.S. tax treaties with foreign countries. The new tax would be prohibited by 18 percent or proposed treaties, and treaties with 8 other countries would prohibit the new tax unless a section 482 type allocation formula were employed to determine the tax.

This conflict with our tax treaties is nowhere mentioned in the House report.

Since most of our treaties are with developed countries, the effect of this conflict would be to cause the new tax to apply primarily to taxpayers from the less-developed countries—unless and until the existing treaties were amended.

You had a concrete example of this pointed out to you earlier this morning by Mr. Kalish when he talked about the problems of banks in Puerto Rico.

An important policy question is, therefore, presented whether the Congress should adopt a provision which would apply in such a discriminatory fashion and against less-developed countries. So far as we are aware, however, this policy question has not yet been examined.

Of particular importance are the very great recordkeeping and compliance burdens which the new provision would place on taxpayers.

First, the provision contains many vague terms which would present difficult interpretative problems in applying them to concrete business situations.

In addition, taxpayers would have to keep complicated and extensive records, records which are not presently necessary for business reasons, in order to comply with the new provision. I might point out for your consideration that this recordkeeping and compliance aspect is described in concrete detail with factual examples on pages 22 to 28 of our report, and I think that portion you might find particularly interesting to read.

Senator ANDERSON. Senator McCarthy just pointed out to me the items on pages 26 and 27, one, two, three, four, up to eight, and two, three, five, two, three, six, eight and on down. Can you explain that to us?

Mr. HENDERSON. That is the example that I was referring to, Senator; yes, indeed.

Senator ANDERSON. What does it mean in connection with this bill?

Mr. HENDERSON. It means in connection with this bill that any foreign taxpayer who would have to determine whether a U.S. tax would apply to his foreign-source income effectively connected with his U.S. office would have to keep a whole new set of records in order to permit his counsel and his accountants and auditors to determine what portion of his income was taxable under this new bill. It means enormous