

tended to attract different meanings to these two subsections, we respectfully suggest a conforming amendment.

4. Similarly, H.R. 13103 and a new subsection b to section 2105 of the Code and a new subsection D to section 861 exempting "deposits with a foreign branch. * * * If such branch is engaged in the *commercial* banking business * * *" from U.S. estate and income taxation. As the present subsection 2105(b) simply requires that the money be deposited with any person "carrying on the banking business", it is not clear whether any change was intended by this new language. The Report of the Committee on Ways and Means is silent in this respect.

5. According to the proposals of H.R. 13103 the revised section 952(b) of the Code would include in Subpart F income an "effectively connected" item of income "exempt from taxation (or * * * subject to a reduced rate of tax) pursuant to a treaty obligation of the United States." In view of the fact that a number of U.S. tax treaties, e.g. U.S. tax treaties with the United Kingdom, Germany and Switzerland, subject income from real property to reduced tax rates both because the statutory rate may be reduced and because the effective rate may be lowered by changing the tax base from gross to net income, and in view of the possible election under section 871(d) and 882(d), this type of income would still fall within the ambit of Subpart F. As there is no apparent reason for this discrimination, it seems probable that it was not intended to except this category of income from the Subpart F exclusion. If this assumption is correct, another reference would have to be added to section 952(b) such as: "Subpart F income also does not include income from real property for which an election is made under section 871(d) or 882(d) or which is subject to net income taxation under a comparable provision in any treaty of the United States."

6. According to the Report of the Committee on Ways and Means (p. 1), H.R. 13103 is intended to revise systematically the U.S. tax treatment of non-resident aliens and foreign corporations. For this reason the meaning of section 872(b) (1) and (2) as well as section 883 should be clarified with respect to the "reciprocity" requirement in view of the fact that two possible criteria are applicable, namely, (a) place of incorporation (or perhaps fiscal residence of a corporation) and (b) place of documentation. The ambiguous state of the present law can best be illustrated by the following example, which assumes that foreign corporation A owns ships documented under the laws of country X and country X grants a tax exemption to U.S. corporations with respect to income from the operation of ships documented in the U.S. As applied to these facts, it is not clear whether section 883 provides that the U.S. on the basis of reciprocity will grant an exemption to corporation A only if A is incorporated under the laws of X or regardless of where it is incorporated? Furthermore, Congress should review the policy objectives of these provisions and then determine how the U.S. would interpret the reciprocity concept if country X in our above example were, for instance, to expand the exemption it grants to U.S. corporations to cover income from the operation of ships regardless of where documented. Would the U.S. want to reciprocate by granting an exemption to corporation A regardless of where it is incorporated or would it rather deny any exemption to corporation A on the theory that the U.S. only wants foreign countries to exempt U.S. corporations with respect to income from the operation of ships documented in the U.S.? Based on present law, these questions cannot be satisfactorily answered so that we respectfully suggest that Congress use this opportunity to clarify these problems.

7. Finally, it is submitted that section 864(b) (2) (A) (ii) should be redrafted so that the statute itself explicitly clarifies the tax treatment of foreign investment companies having their principal office within the U.S. This would make it unnecessary to refer to the legislative history which, at present, is the only source dealing with this problem.

II. SUGGESTIONS FOR SUBSTANTIVE CHANGES IN H.R. 13103

1. "Effectively connected" concept

H.R. 13103 introduces the new concept of "effectively connected" income as a means to—

(1) distinguish between business and investment income, and

(2) determine the amount of business income that is subject to the regular progressive U.S. tax rates.

According to the legislative history of this bill, the first purpose was to encourage foreign investment in the U.S. by having investment income taxed at only 30