

resident aliens has been to prevent the avoidance of the graduated rates of U.S. tax applicable to certain nonresident alien individuals by utilizing foreign holding companies as the recipients of their U.S. source investment income. Generally the graduated rates presently apply when a nonresident alien's U.S. gross income exceeds \$21,200 or when he is engaged in a trade or business in the United States. However, under your committee's and the House bill nonresident aliens are not to be subject to the graduated rates of tax unless their income is effectively connected with a trade or business in the United States. In view of this the retention of the personal holding company tax would appear to serve no purpose where all of the shareholders are nonresident aliens.

Explanation of provision.—The House bill modifies the provision in present law excluding from the personal holding company definition only those foreign corporations which meet two tests; namely, where their U.S. source gross income is less than 50 percent of their total gross income and all of their stock is held directly or indirectly by nonresident aliens. In place of this the House bill substitutes a broader exemption which applies to any foreign corporation all of whose outstanding stock during the last half of its taxable year is owned by nonresident alien individuals (directly or indirectly through foreign estates, trusts, partnerships, or other foreign corporations).

Your committee has adopted three amendments in this area. The first amendment provides that the general exclusion from the personal holding company provision provided in the House bill is not to be available to a foreign corporation which is a personal holding company if it has income from personal services which is personal holding company income described in section 543(a)(7). In such a case the personal holding company tax is to be assessed on that personal service income. The second amendment provides a de minimus rule, in addition to the general exception provision provided in the House bill. Under the amendment, in the case of foreign corporations with only 10 percent or less U.S. ownership the personal holding company tax is to be assessed only on the corporation's undistributed personal holding company income attributable to the U.S. shareholders' interest. The final amendment adopted by your committee provides that a foreign corporation can claim all appropriate deductions in computing its personal holding company tax notwithstanding the general rule disallowing deductions where no return is filed. However, a 10-percent addition to taxes otherwise due is to be assessed.

Effective date.—This amendment applies with respect to taxable years beginning after December 31, 1966.

f. Foreign corporations carrying on insurance business in the United States (sec. 104(i) of the bill and secs. 819, 821, 822, 831, 832, 841 and 842 of the code)

Present law.—Present law taxes a foreign life insurance company carrying on a life insurance business in the United States on all its income attributable to that business in substantially the same manner as a domestic life insurance company.³ Foreign insurance companies carrying on life insurance businesses in the United States gen-

³ A foreign life insurance company that is not carrying on a life insurance business in the United States is taxable under the provisions applicable to foreign corporations generally.