

the denial of the credit to such persons under these circumstances is unjustified and, therefore, has amended present law so as to allow these persons the foreign tax credit unless the President finds that so doing is not in the public interest.

*Explanation of provision.*—The bill modifies the provision of present law which in all cases denies a credit for citizens of a foreign country if it does not provide reciprocity for U.S. citizens residing there. Under the bill the President is given some discretion as to the disallowance of the credits in such cases. The bill provides that the President is to deny a foreign tax credit to residents who are subjects of a foreign country if he finds: (1) That a foreign country, in imposing income, war profits, and excess profits taxes or death taxes does not allow U.S. citizens residing in that country a credit for any taxes paid or accrued to the United States or any foreign country, similar to the foreign tax credit allowed by the United States to subjects of that foreign country residing in the United States; (2) that the foreign country, when requested to do so, has not acted to provide a similar credit to U.S. citizens residing in that foreign country; and (3) that it is in the public interest to allow the U.S. foreign tax credit to citizens or subjects of the foreign country who reside in the United States only if the foreign country allows such a similar credit to citizens of the United States residing in the foreign country.

The disallowance of the credit in any such case is to apply for taxable years beginning while a Presidential proclamation denying the credit is in effect.

*f. Separate foreign tax credit limitation (sec. 106(c) of the bill and sec. 904(f) of the code)*

*Present law.*—Generally, under present law the limitation on the allowable foreign tax credit, must be computed separately for all interest income and on a “per country” basis. The exceptions to this general rule are for:

(1) Interest derived from any transactions directly related to the active conduct of a trade or business in a foreign country or U.S. possession;

(2) Interest derived in the conduct of a banking, financing, or similar business (such as an insurance company business);

(3) Interest received from a corporation in which the taxpayer owns at least 10 percent of the voting stock; and

(4) Interest received on obligations acquired as the result of the disposition of a trade or business actively conducted by a taxpayer in a foreign country or as a result of a disposition of stock or obligations of a corporation in which the taxpayer owned at least 10 percent of the voting stock.

This provision was added to the code by the Revenue Act of 1962 so as to foreclose the transfer outside the United States (primarily to Canada) of short-term funds, such as bank deposits, in order to make it possible to use foreign tax credits, which otherwise could not be used, to reduce the U.S. tax on a domestic corporation’s worldwide income. Interest income previously could be used in this manner because typically the foreign tax on such income was below the regular corporate tax which would apply to interest income received by a domestic corporation. Thus, if the overall limitation were used there