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DIGEST OF TESTIMONY PRESENTED
AND STATEMENTS SUBMITTED TO
THE COMMITTEE ON WAYS AND MEANS
WITH RESPECT TO H.R. 8000
("INTEREST EQUALIZATION TAX ACT OF 1963")

PREPARED FOR THE USE OF THE
COMMITTEE ON WAYS AND MEANS
HOUSE OF REPRESENTATIVES
BY THE STAFF OF
THE JOINT COMMITTEE ON INTERNAL
REVENUE TAXATION



OCTOBER 21, 1963

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INTRODUCTION

On August 20, 21, 22, and 23, 1963, the Committee on Ways and Means held public hearings on H.R. 8000, the "Interest Equalization Tax Act of 1963."

This digest attempts to summarize the arguments advanced for and against the bill. In general, the arguments advanced for the bill are summarized in section I, and the arguments advanced against the bill are summarized in section II. Recommendations for basic modification of the bill are summarized in section III, while more specific recommendations are set forth in a section-by-section analysis in section IV. Finally, specific alternative recommendations made by witnesses are summarized in section V.

An attempt has been made to summarize generally all arguments and recommendations; however, if some testimony has been omitted, it was unintentional. For detailed statements presented by witnesses and by those whose statements were submitted for the record, it is necessary to refer to the printed hearings.

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I. SUMMARY OF TESTIMONY RECOMMENDING ENACTMENT OF H.R. 8000

Comments	Name of witness														
<p>A. Reasons for imposition of an interest equalization tax:</p> <p>(1) Imposition of the tax will reduce the immediate strains placed on the U.S. balance-of-payments position by an increased outflow of long-term portfolio capital from this country.</p> <p>(a) In recent years there has been an increase in the U.S. balance-of-payments deficit position on regular transactions.</p> <table border="1" style="width: 100%; border-collapse: collapse; margin-top: 10px;"> <thead> <tr> <th style="width: 40%; text-align: center;">Year</th> <th style="width: 60%; text-align: center;">Deficit on "regular transactions" (approximate amount in billions)</th> </tr> </thead> <tbody> <tr> <td>1961.....</td> <td style="text-align: center;">\$3</td> </tr> <tr> <td>1962.....</td> <td style="text-align: center;">3½</td> </tr> <tr> <td>1963 (annualized).....</td> <td style="text-align: center;">4</td> </tr> </tbody> </table> <p>(b) The increased deficit on regular transactions is due almost entirely to the accelerating outflow of long-term portfolio capital into new issues of foreign securities.</p> <table border="1" style="width: 100%; border-collapse: collapse; margin-top: 10px;"> <thead> <tr> <th style="width: 40%; text-align: center;">Year</th> <th style="width: 60%; text-align: center;">Increase in U.S. purchases of new foreign securities over preceding year (millions)</th> </tr> </thead> <tbody> <tr> <td>1962.....</td> <td style="text-align: center;">\$553</td> </tr> <tr> <td>1963 (annualized).....</td> <td style="text-align: center;">1 875</td> </tr> </tbody> </table>	Year	Deficit on "regular transactions" (approximate amount in billions)	1961.....	\$3	1962.....	3½	1963 (annualized).....	4	Year	Increase in U.S. purchases of new foreign securities over preceding year (millions)	1962.....	\$553	1963 (annualized).....	1 875	<p>Treasury Department. American Federation of Labor and Congress of Industrial Organizations. Smith, Kline & French Overseas Co.</p>
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1963 (annualized).....	1 875														

¹ Estimated.

I. SUMMARY OF TESTIMONY RECOMMENDING ENACTMENT OF H.R. 8000—Continued

Comments	Name of witness
<p>(2) The tax should bring the cost of capital raised by foreigners in the U.S. market into closer alinement with costs prevailing in the markets of most other industrialized countries.</p> <p style="padding-left: 20px;">(a) The major reason foreigners have increased their borrowings in New York has been the ready availability of funds at a relatively low interest rate, rather than a pressing need for capital from outside the borrower's own country.</p> <p style="padding-left: 20px;">(b) Foreign governments have recently been borrowing substantially more in the United States than they did in earlier years. Moreover, there has been a sudden rise in sales of new issues by foreign corporations.</p> <p>(3) Imposition of the tax will give the United States time to make fundamental adjustments in other areas.</p> <p style="padding-left: 20px;">(a) Action has been taken to reduce the rate of Government over-sea spending by \$1 billion within the next 18 months.</p> <p style="padding-left: 20px;">(b) The tax program (H.R. 8363) will not be immediately effective in reducing the U.S. balance-of-payments deficit.</p> <p>(4) Imposition of the tax will encourage other industrialized countries to develop their own capital markets.</p> <p>B. Reasons for principal exemptions and exclusions from tax.</p> <p>(1) Short-term capital:</p> <p style="padding-left: 20px;">(a) Imposition of the tax on short-term capital could impede the normal flow of commerce.</p> <p style="padding-left: 20px;">(b) Shifts of short-term funds in response to interest rate differentials cannot readily be distinguished from other commercial transactions.</p> <p>(2) Direct investments in 10-percent-owned subsidiaries:</p> <p style="padding-left: 20px;">(a) In-making such investments, questions of market position and long-range profitability outweigh any concern over interest rate differentials.</p> <p>(3) Investments in less-developed countries;</p>	

(a) There should be no impediment to the flow of private capital to nations with capital shortages and urgent development needs.

(4) Authorization to exclude certain new issues:

(a) The President's authority under this provision should be exercised only in response to highly unusual circumstances.

(b) Under existing circumstances, the exemption should apply only in the case of Canada. However, the provision should not be amended by specifically enumerating the countries to be eligible for the exclusion or by limiting more narrowly the President's discretion to grant the exclusion.

(5) Export credit

(a) Imposition of the tax should not adversely affect U.S. exports. However, consideration should be given to the effect of the tax on Webb-Pomerenche-type associations, export merchants, and "turnkey" arrangements.

C. Reasons for rejecting alternative proposals.

(1) A sharp rise in long-term interest rates would reduce both domestic and foreign borrowing. Such a proposal would increase domestic unemployment and jeopardize the prospects for restoring lasting balance in our international accounts.

(2) The balance-of-payments problem cannot be met simply by exercising the moral force of Government leadership and persuasion. Firm legal guidelines and discipline of market forces are required to reinforce these efforts.

(3) The effectiveness of the tax would be sharply reduced if outstanding securities were excepted from the tax.

(a) In 6 of the past 10 years there has been a drain on the U.S. balance-of-payments position from the purchases of outstanding foreign stocks by U.S. persons. The drain amounted to \$326 million in 1961.

(4) Exemption of new issues of stocks from tax would impair the effectiveness of the tax.

(a) Bonds and stocks represent alternative sources of funds and it would be inconsistent to tax foreign access to one market and not the other.

Department of State.

Department of Commerce.

Summary of recent capital transactions with Europe

Year	Excess of European purchases of U.S. securities over U.S. purchases of European securities (millions)
1958-62.....	\$280
1963 (5 months).....	(23)

Source: Testimony of Investment Bankers Association, pp. 221, 222.

(4) H.R. 8000 will not make a significant contribution toward reduction of the U.S. balance-of-payments deficit.

(a) Because of various exceptions and exclusions, H.R. 8000 would, at a maximum, effect a reduction of approximately \$300,000,000 annually in the U.S. balance-of-payments deficit:

Net recorded purchases of foreign securities by U.S. institutions, citizens, and residents

(Millions)

	1958	1959	1960	1961	1962	1963 (5 months)
Total purchases of stocks and bonds.....	\$1,362.5	\$749.7	\$644.7	\$830.4	\$1,047.9	\$585.9
Exclusion for international institutions.....		156.6	147.0	1.3	165.3	119.4
Total.....		593.1	497.7	831.7	882.6	466.5
Other exclusions and exemptions.....			381.2	519.7	583.5	370.0
Amount subject to tax.....			116.5	312.0	299.1	96.5

Source: Testimony of International Investment Analysts, p. 297.

Burnham & Co.
 Investment Bankers Association.
 Investors League, Inc.
 Model, Roland & Co.
 Morgan Stanley & Co.
 International Bond & Share, Inc.
 International Investment Analysts.
 Smith, Barney & Co.

II. SUMMARY OF TESTIMONY AGAINST ENACTMENT OF H.R. 8000—Continued

Comments	Name of witness or association
<p>H.R. 8000, etc.—Continued</p> <p>(b) Foreign borrowers may switch from long-term debt and equity financing to short-term or bank-loan financing as a means of avoiding the tax.</p> <p>(c) Due to the fact interest rate differentials between countries are not uniform, some foreign borrowers will find it cheaper to borrow in the United States and pay the interest equalization tax than pay the interest rates applicable to loans made in foreign countries.</p> <p>(d) If an investment decision is based upon current rate of return, the bill may have some effect; however, if the motive is to participate in growth situations, the tax will have no appreciable influence on investment decisions.</p> <p>(5) Enactment of H.R. 8000 may cause an increase in the U.S. balance-of-payments deficit.</p> <p>(a) Enactment of H.R. 8000 will lessen confidence in the dollar—</p> <p style="padding-left: 20px;">(i) Foreigners may sell their holdings of U.S. securities.</p>	<p>Burnham & Co. International Bond & Share, Inc. International Investment Analysts. Investment Bankers Association. Model, Roland & Co. Morgan Stanley & Co. B. F. Pitman, Jr. Smith, Barney & Co. Stein Roe & Farnham. Hon. John A. Burns, Governor of the State of Hawaii. Machinery & Allied Products Institute. B. F. Pitman, Jr. United States Trust Co. of New York. International Economic Policy Association.</p> <p>Bache & Co. Carl Marks & Co. International Bond & Share, Inc. Madison Fund, Inc. Wertheim & Co.</p> <p>Burnham & Co. International Investment Analysts. Investment Bankers Association. Investors Diversified Services. Model, Roland & Co. Morgan Stanley & Co. National Association of Security Dealers, Inc.</p>

(ii) Long-term borrowers who seek to make loans in a weak currency will be encouraged to make U.S. dollar loans. Investors fearing devaluation of the dollar will continue to invest in foreign securities.

(iii) A dual price structure on securities will indicate a weakness of the dollar.

(b) U.S. exports which are tied to U.S. borrowings will decline.

(c) Foreign countries may retaliate. For example, Japan may impose restrictions on importation of U.S. goods and limit foreign travel of its citizens.

New York Chamber of Commerce.
Smith, Barney & Co.
J. R. Timmins & Co.
United States Trust Co. of New York.
International Economic Policy Association.
B. F. Pitman, Jr.

Investment Bankers Association.
Investors Diversified Services.
Smith, Barney & Co.
Stein Roe & Farnham.
American Life Convention & Life Insurance Association
of America.
Bank of Hawaii.
Investment Bankers Association.
Investors Diversified Services.
Japan Bond Underwriters Association.
Japan Federation of Securities Dealers' Association.
Kidder, Peabody & Co.
Morgan Stanley & Co.
National Association of Manufacturers.
Raymond Rodgers.
Smith, Barney & Co.
United States Trust Co. of New York.
American Life Convention & Life Insurance Association
of America.
Bank of Hawaii.
Hon. John A. Burns, Governor of the State of Hawaii.
First National Bank of Hawaii, Henry J. Clay.
Hon. Hiram J. Fong, U.S. Senator from the State of
Hawaii.
Machinery & Allied Products Institute.
Madison Fund, Inc.
New York Chamber of Commerce.
Pineapple Growers Association of Hawaii.
Raymond Rodgers.
J. R. Timmins & Co.

III. SUMMARY OF TESTIMONY RECOMMENDING BASIC MODIFICATIONS OF H.R. 8000

Comments	Name of witness or association
<p>A. Acquisitions which have no adverse effect on the U.S. balance-of-payments position should be exempt from tax.</p>	<p>Cravath, Swaine & Moore. Morgan Stanley & Co. J. R. Timmins & Co.</p>
<p>(1) U.S. persons who own foreign securities should be permitted to switch from one foreign security to another foreign security without imposition of a tax.</p>	
<p>(a) Provision should be made to permit dollar amounts received from the sale of foreign securities by U.S. persons to foreign persons to be reinvested in foreign securities by the U.S. person making the sale or any other U.S. person without imposition of a tax. Such transactions have no net effect on the U.S. balance-of-payments position.</p>	<p>American Institute of Certified Public Accountants. Carl Marks & Co. Henry J. Clay. International Investors, Inc. National Association of Security Dealers, Inc.</p>
<p>(b) Allowance should be made to permit a U.S. person to switch his investment in foreign securities from one investment to another without imposition of a tax.</p>	<p>Burnham & Co. Investment Company Institute. Morgan Stanley & Co. National Association of Manufacturers. J. R. Timmins & Co. Wertheim & Co. Burham & Co.</p>
<p>(i) Switching in this manner would have no net effect on the U.S. balance-of-payments position.</p>	
<p>(ii) By limiting the switch privilege to the person selling a security, the exemption would not be interpreted as a form of devaluation of the dollar for the following reasons:</p>	<p>Burnham & Co.</p>
<p>(a) The switch transactions would primarily be accomplished in foreign currencies; therefore, the U.S. dollar would not be affected.</p>	
<p>(b) By prohibiting the transfer of "investment dollars," the approach would be consistent with that followed by Japan when, until Apr. 1, 1963, it required that proceeds from the sale of securities acquired with a permit from the Japanese authorities be retained in Japan. Limitation of the switch privilege to the person who sold a foreign security would avoid the creation and marketability of "in-</p>	

vestment dollars". Multiple rate situations occurred in the United Kingdom, Germany, France, and the Netherlands only because a form of investment dollar was freely transferable.

(2) Security transactions resulting in the financing of exports should be exempted.

(a) The Treasury figures for the first half of 1963 show U.S. purchases of Western European securities amounting to \$205 million. During this period, Morgan Stanley & Co. managed or comanaged Western European issues totaling \$172.5 million. Approximately, \$160 million of the proceeds of these financings were spent in the United States and did not affect the U.S. balance of payments. A simple procedure could be established to insure that such funds do not leave the United States, in which case such transactions should be exempt from tax.

(3) Domestic insurance companies operating abroad should be allowed to invest premiums collected abroad in foreign securities without payment of the tax.

(a) Premiums must be invested in the currency of the country in which collected, since it is generally unsound to force an insurance company to assume the exchange risk of converting premiums to dollars for investment purposes and then back to a foreign currency for payment purposes.

(4) Labor unions operating abroad should be allowed to invest union dues collected abroad in foreign securities without payment of the tax.

(5) Purchase of foreign securities by U.S. citizens abroad should be exempt from tax.

(a) Purchase of stock by an employee under an employer-sponsored purchase plan should be exempt.

(b) Exemption could be limited to persons who are bona fide residents abroad.

(c) Acquisition of stock options, or acquisition of stock pursuant to the exercise of a stock option, by a U.S. person who is an employee of the issuing corporation, its parent or its subsidiaries, should be exempt from tax if the option is acquired in connection with his employment and the stock is acquired without an intent of offering the stock for sale to a U.S. person.

Investment Bankers Association.
Kidder, Peabody & Co.
Smith, Barney & Co.
Morgan Stanley & Co.

American Life Convention & Life Insurance Association
of America.

American Federation of Labor & Congress of Industrial
Organizations.
Brotherhood of Railroad Trainmen.
U.S. Council of the International Chamber of Commerce,
Inc.
Standard Oil Co. (New Jersey).
U.S. Chamber of Commerce.
Canadian Husky Oil, Ltd.
Standard Oil Co. (New Jersey).
Canadian Husky Oil, Ltd.
Roberts & Holland.

III. SUMMARY OF TESTIMONY RECOMMENDING BASIC MODIFICATIONS OF H.R. 8000—Continued

Comments	Name of witness or association
<p>Acquisition, etc.—Continued</p>	
<p>(6) Foreign subsidiaries of U.S. parent corporations should be permitted to borrow U.S. dollars free of tax if the proceeds of the loan are to be returned to the United States through the retirement of an outstanding loan with the U.S. parent.</p>	<p>B. F. Goodrich Co.</p>
<p>(7) Investments in foreign corporations having 80 percent or more of their assets invested in U.S. property should be fully exempt from tax.</p>	<p>Roberts & Holland.</p>
<p>(8) Acquisition of foreign securities by domestic corporations whose stock is more than two-thirds owned by foreigners should be exempt from tax due to the fact—</p>	<p>International Holdings Co.</p>
<p>(i) there is no dollar drain since the funds invested were originally derived from foreign sources;</p>	
<p>(ii) the exemption would apply only to reinvestment of proceeds of sales of foreign securities; and</p>	
<p>(iii) the United States would lose the 30 percent withholding tax and tax on capital gains if the domestic corporation reincorporated as a foreign corporation.</p>	
<p>(9) Trading in stock of a foreign corporation should be exempt from tax so long as the foreign corporation invests an amount in the United States equal to the dollar value of its stock held by Americans.</p>	<p>Carling Brewing Co.</p>
<p>(10) Arbitrage transactions should be permitted without imposition of tax if the proceeds are reinvested by the arbitrageur within a stated period of time.</p>	<p>Smith, Barney & Co.</p>
<p>B. H.R. 8000 should not apply to purchases of outstanding securities.</p>	<p>Carl Marks & Co. New York Stock Exchange. Smith, Barney & Co. United States Council of the International Chamber of Commerce, Inc. Wertheim & Co.</p>

(1) For 1962 and for the 1st half of 1963, acquisitions of outstanding foreign securities by U.S. persons has been approximately offset by acquisition of U.S. securities by foreigners.

(2) Since 1950, foreigners have purchased more U.S. corporate securities than U.S. persons have purchased outstanding foreign securities:

Year	Net inflow of dollars to the United States (excluding net foreign purchases of U.S. governments) (millions)
1950.....	\$(319)
1951.....	159
1952.....	171
1953.....	293
1954.....	120
1955.....	140
1956.....	181
1957.....	153
1958.....	(380)
1959.....	310
1960.....	105
1961.....	(8)
1962.....	79
1963 (1st quarter).....	(19)
Total.....	935

¹ Estimated.

Source: Testimony of New York Stock Exchange, p. 438.

Burnham & Co.
International Investment Analysts.
Investment Bankers Association.
Madison Fund, Inc.
Model, Roland & Co.
Morgan Stanley & Co.
National Association of Security Dealers, Inc.
Stein Roe & Farnham.
United States Trust Co. of New York.
New York Stock Exchange.

III. SUMMARY OF TESTIMONY RECOMMENDING BASIC MODIFICATIONS OF H.R. 8000—Continued

Comments	Name of witness or association																				
<p>B. H.R. 8000, etc.—Continued</p> <p>(3) Exemption for outstanding securities would not result in a switching of investments by U.S. persons from new to outstanding issues:</p> <p>(a) Unregistered securities may not be resold in the United States until foreign distribution has been completed.</p> <p>(b) Different type investors buy new as compared with outstanding issues. Institutional investors generally buy new issues while smaller investors generally buy outstanding issues.</p>	<p>Investment Bankers Association.</p> <p>Model, Roland & Co.</p>																				
<p>C. H.R. 8000 should not apply to new issues of stock.</p> <p>(1) Dollar outflow from sales of new foreign stock issues has been a relatively small amount when compared with the outflow resulting from sales of bonds:</p> <p style="text-align: center;">[Millions]</p>	<p>Morgan, Stanley & Co.</p> <p>Stein Roe & Farnham.</p>																				
<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 60%;"></th> <th style="width: 10%;">1960</th> <th style="width: 10%;">1961</th> <th style="width: 10%;">1962</th> <th style="width: 10%;">1st quarter, 1963</th> </tr> </thead> <tbody> <tr> <td>Long-term loans by institutions.....</td> <td style="text-align: right;">\$200</td> <td style="text-align: right;">\$258</td> <td style="text-align: right;">\$248</td> <td style="text-align: right;">(\$14)</td> </tr> <tr> <td>New foreign bonds after deducting redemptions.....</td> <td style="text-align: right;">459</td> <td style="text-align: right;">364</td> <td style="text-align: right;">832</td> <td style="text-align: right;">456</td> </tr> <tr> <td>New foreign stocks.....</td> <td style="text-align: right;">14</td> <td style="text-align: right;">36</td> <td style="text-align: right;">74</td> <td style="text-align: right;">25</td> </tr> </tbody> </table>		1960	1961	1962	1st quarter, 1963	Long-term loans by institutions.....	\$200	\$258	\$248	(\$14)	New foreign bonds after deducting redemptions.....	459	364	832	456	New foreign stocks.....	14	36	74	25	
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New foreign bonds after deducting redemptions.....	459	364	832	456																	
New foreign stocks.....	14	36	74	25																	
<p>(2) Exemption of stocks from the tax should not result in a switch of investment from bonds to stock for two reasons. First, many institutional investors who buy foreign debt obligations do not typically buy foreign equity securities and, second, many large foreign issuers have been public or quasi-public bodies which do not issue common stocks.</p>	<p>Do.</p>																				

D. H.R. 8000 should not apply to Canadian securities.

(1) The bill should not apply to acquisition of stock in foreign corporations which are 50 percent owned by U.S. persons if the stock is listed on a national stock exchange since trading in such stock does not adversely affect the U.S. balance-of-payments position.

(2) Acquisitions of all Canadian securities listed on a national stock exchange should be exempt from tax.

(a) This provision would add seven Canadian companies to those covered by item (1).

(b) Trading of these shares since 1961 has resulted in a net inflow of dollars to the United States.

(3) Acquisition of any Canadian security should be exempt from tax.

(a) Canada has an unfavorable trade balance with the United States. For the years 1958-62, this deficit totaled just under \$3 billion.

(b) For 1962 and the first 5 months of 1963, Canadians have been net purchasers of outstanding stock:

	1962 (millions)	5 months, 1963 (millions)
Purchases by Canada from the United States.....	\$554.7	\$191.5
Sales by Canada to the United States.....	543.1	136.1
Total.....	11.6	55.4

E. Any transaction which is directly related to the active conduct of a trade or business abroad should be exempt from tax.

(1) Business loans are generally made as a result of competition with foreign companies and not because of interest return or other purely financial considerations.

International Nickel Corp.

Do.

Investors League, Inc.

A. E. Ames & Co.
Grace Canadian Securities, Inc.
J. R. Timmins & Co.

National Association of Manufacturers.
National Foreign Trade Council, Inc.
Raymond Rodgers.
Standard Oil Co. (New Jersey).
United States Council of the International Chamber of Commerce.

IV. SECTION-BY-SECTION ARRANGEMENT OF COMMENTS

Section 4911. Imposition of Tax

Subsection (a) imposes a tax on the acquisition by U.S. persons of debt obligations of foreign obligors. The rate of tax increases from 2.75 percent of actual value for obligations with maturities of at least 3 years but less than 3½ years to 15 percent for obligations with maturities exceeding 28½ years. The tax does not apply to debt obligations having a maturity of less than 3 years.

COMMENTS

See sections II and III.

* * * * *

The principle of interest equalization should be applied to U.S. controlled Euro-dollars.—Bache & Co.

* * * * *

A refund procedure should be available when a note is prepaid.—Association of the Bar of the City of New York

* * * * *

The tax should not apply to an interest bearing note received by a U.S. person upon sales of assets by him to a foreigner under a deferred payment contract.—Martin D. Ginsburg.

* * * * *

Under certain circumstances it may be impossible to determine the duration of a loan at the time it is made. For example, if repayment is dependent upon percentage payments out of the proceeds of a banana crop, it is impossible to tell when a note will be paid.—United Fruit Co.

Subsection (b) imposes a tax on the acquisition of stock of a foreign issuer by a U.S. person. The tax is equal to 15 percent of the actual value of the stock.

COMMENTS

See sections II and III.

Subsection (c) provides that the person acquiring the security shall pay the tax.

NO COMMENTS

Subsection (d) provides that the tax shall not apply to acquisition made after December 31, 1965.

NO COMMENTS

Section 4912. Acquisitions

Subsection (a), in general, defines the term "acquisition" to mean any purchase, transfer, distribution, exchange, or other transaction by virtue of which ownership of a foreign security is obtained by a U.S. person. An extension or renewal of an existing debt obligation is treated as a new obligation.

COMMENTS

The period remaining to maturity of a debt obligation should be measured from the date the loan is actually made rather than from the date the obligation becomes unconditionally binding on the parties.—National Association of Manufacturers.

* * * * *

Imposition of tax and maturity of a debt obligation should depend on the date funds are transferred rather than on the date the loan agreement becomes binding on the parties.—American Institute of Certified Public Accountants.

* * * * *

If an outstanding loan has a history of being renewed, or the parties to the loan contemplated that the agreement would be renewed at the time it was made, the tax should not be imposed if it is renewed.—National Foreign Trade Council, Inc.

Subsection (b) provides special rules.

Paragraph (1) of subsection (b) provides that transfers of money or other property to a foreign trust, partnership, or estate is taxable to the extent the foreign entity acquires stock or debt obligations of a foreign issuer or obliger.

COMMENTS

The tax should be based on the U.S. person's percentage share of the foreign obligations acquired by the foreign trust, partnership or estate rather than the total amount acquired. For example, if a foreign partnership invested \$1,000 if its \$10,000 capital in stock of a foreign corporation, and \$9,000 in a manufacturing plant, the amount subject to tax in the hands of a 10 percent partner should be \$100, not \$1,000.—Association of the Bar of the City of New York.

* * * * *

The exemptions applicable to direct investments in 10 percent owned subsidiaries and investments in less developed country corporations should apply to U.S. persons taxed under this section in the same manner as if the investments were made directly.—Association of the Bar of the City of New York.

Paragraph (2) of subsection (b) provides that a transfer to capital of a corporation is to be treated as an acquisition of stock.

NO COMMENTS

Paragraph (3) of subsection (b) provides that acquisitions of foreign securities in connection with corporate reorganizations or distributions are considered as being acquired from the issuer or obligor of the foreign security.

COMMENTS

Exemption under this provision should not depend on receipt of a tax-free ruling under section 367 of the Internal Revenue Code as is implied from the Treasury Department technical explanation of the bill—Association of the Bar of the City of New York.

Section 4913. Limitation on Tax on Certain Acquisitions

Subsection (a) provides that tax at the time of the exercise of an option, or the extension or renewal of a debt obligation, is to be limited as provided in subsection (b).

COMMENTS

Exchanges in bankruptcy or insolvency situations should be exempt from tax.—Association of the Bar of the City of New York.

Subsection (b) provides that the tax on the exercise of an option, or extension or renewal of a debt obligation, is to be determined by reducing the tax payable under the general rule by the tax which would have been payable had the option or security surrendered been subject to tax immediately before the time of exercise, renewal, etc. In the case of certain defaulted Government obligations, the bill provides for their tax-free exchange.

NO COMMENTS

Section 4914. Exclusion for Certain Acquisitions

Subsection (a) provides, in general, that the tax shall not apply to the following transactions:

1. Transfers between a person and his nominee, custodian, or agent;
2. Certain transfers by operation of law;
3. Gifts and inheritances;
4. Distributions and exchanges of stock by a corporation to or with its shareholders; or
5. Conversion of debentures into stock.

COMMENTS

Provision should be made to exempt acquisitions by an existing shareholder under a subscription solely for the purpose of maintaining his proportionate equity.—Westinghouse Electric Corp.

Subsection (b) provides that the following U.S. persons are not subject to tax.

- (1) Agencies and instrumentalities of the United States.

NO COMMENTS

(2) Commercial banks making loans in the ordinary course of their commercial banking business.

COMMENTS

Exemption should be limited to strictly commercial credit transactions or to the financing of specific export transactions.—Smith, Barney & Co.

* * * * *

The statute should specifically provide for exemption of foreign securities acquired by Edge Act corporations.—New York Clearing House.

(3) Exporters of U.S. goods are exempt from tax if the goods exported were manufactured, produced, extracted, or grown in the United States by the exporter or a related corporation. However, this exemption applies only if the debt obligation is held to maturity by the exporter or is transferred by him to a commercial bank or agency or instrumentality of the United States.

COMMENTS

Proceeds from the sale of any security should be exempt to the extent used to purchase goods or services from U.S. persons—Investment Bankers Association.

* * * * *

Exemption should apply to export transactions dealing wholly or in part with services since such services are almost inevitably a part of a transaction involving the sale of products—Machinery & Allied Products Institute.

* * * * *

Provision should be made to exclude debt obligations of a foreign issuer received by a foreign branch of a domestic corporation as a result of the sale of goods produced abroad by the foreign branch—Association of the Bar of the City of New York.

* * * * *

A U.S. exporter who undertakes to provide a purchaser with a complete operating facility should be allowed to receive debt obligations of the foreign issuer free of tax. Failure to provide exemption will place U.S. companies at a price disadvantage. Moreover, allocation of a portion of the purchase price of such contracts to U.S. manufactured goods could become hopelessly involved—Westinghouse Electric Corp.

* * * * *

“Turnkey” contracts (contracts where a U.S. manufacturer assumes responsibility for an entire project of which his equipment is only part) should be excepted from the tax—National Association of Manufacturers.

* * * * *

In order to be competitive with foreign contractors, the bill should be amended to exclude from tax debt obligations and stock received as compensation for services, material, machinery, equipment, construction, or any combination of them, performed, furnished, procured, or supplied by the U.S. person or his subcontractor—National Constructors Association.

* * * * *

Provision should be made to permit dispositions because of factors beyond the control of the exporter, for example reorganizations, bankruptcy, etc.—National Association of Manufacturers.

* * * * *

A U.S. person should be permitted to transfer a debt obligation to a controlled foreign corporation which qualifies as an export trade corporation.—Westinghouse Electric Corp.

(4) Any U.S. person is exempt from tax to the extent acquisition of foreign securities is reasonably necessary to satisfy minimum requirements imposed upon him by foreign law. Foreign law requirements are, in effect, frozen as of July 18, 1963.

COMMENTS

Test should be whether the stock or debt obligation was acquired "in accordance with good business practice" in a foreign country.—National Foreign Trade Council, Inc.

* * * * *

The exemption for investments required by foreign law should permit all investments made pursuant to any legal requirement so long as it is not discriminatory against American corporations. U.S. banks operating foreign branches have no choice but to comply with laws of the countries in which they operate.—New York Clearing House.

* * * * *

It is customary for insurance companies to invest premiums collected abroad in securities of the foreign country in which collected. Therefore, investments in excess of legal requirements are a matter of business necessity, even though not compelled by law. It is also unrealistic and unfair to restrict investments to those required by foreign insurance laws as they existed on July 18, 1963—Association of Casualty & Surety Companies and the National Board of Fire Underwriters.

* * * * *

Some countries do not require investment in the securities of that country but the need to keep money in the country of origin nevertheless exists. Moreover, due to market fluctuations, it is not possible to maintain a level of investment exactly equal to that required (some life insurance companies keep a surplus of not more than 10 percent)—American Life Convention and Life Insurance Association of America.

* * * * *

Restriction of investments to a required reserve is too narrow. Provision should also be made to allow for changes in requirements imposed by foreign governments—American Foreign Insurance Association.

Section 4915. Exclusion for Direct Investments

Subsection (a) provides, in general, that the tax does not apply to acquisitions by U.S. persons of securities of a foreign corporation in which they own, directly or indirectly, a 10-percent or greater stock interest.

COMMENTS

The 10-percent figure is too high. The exemption should turn on whether the foreign corporation whose stock is acquired is engaged in operations similar or related to those of the investor—Chamber of Commerce of the United States.

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The 10-percent figure is too high. The exemption should apply to investments in corporations in a related business—Standard Oil Co. (New Jersey).

* * * * *

The 10-percent ownership requirement is too high to provide an adequate basis for distinction between portfolio investments and direct investments. Investments of lesser amounts should be exempt if made in corporations engaged in operations similar or related to those of the investor—United States Council of International Chamber of Commerce, Inc.

* * * * *

Broader stock attribution rules than those provided should be adopted for purposes of determining if a person owns 10 percent of the stock of a foreign corporation—Association of the Bar of the City of New York.

* * * * *

Exemption should be provided in cases where a U.S. contractor, in order to comply with the terms of a bid on a construction contract, obtains less than a 10-percent interest in a foreign corporation. Such bid requirements have recently been imposed by some foreign purchasers of large-scale projects to insure that major contractors retain an interest in the project after performance has been completed.—Westinghouse Electric Corp.

* * * * *

Provision should be made to grant refund of tax paid with respect to acquisitions while owning less than 10 percent of the stock of the foreign corporation if the U.S. person subsequently acquires a 10-percent interest in the corporation.—National Association of Manufacturers.

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Provision should be made to exempt investments made through partnerships or other forms of business organizations.—National Association of Manufacturers.

* * * * *

Provision should be made to provide that any member of an affiliated group can make loans to foreign subsidiaries in those cases where the foreign subsidiary is 10 percent owned by a U.S. corporate member of the affiliated group.—United Fruit Co.

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Provision should be made to allow U.S. persons generally to make tax-free loans to 10-percent-owned foreign subsidiaries of domestic corporations—Kaiser Aluminum & Chemical Corp.

* * * * *

If the U.S. persons who own a domestic corporation also own a foreign corporation, the domestic corporation should be permitted to make tax-free loans to the foreign corporation.—Stephen S. Ziegler.

* * * * *

Committee report should make it clear that a 10-percent interest need not be acquired at one time for the exception to apply.—United States Gypsum Co.

Subsection (b) provides that the direct investment rule of subsection (a) does not apply to corporations which are formed or availed of for the purpose of acquiring securities of a foreign corporation, which if acquired directly, would be subject to tax. However, this provision does not apply to corporations formed or availed of to hold foreign securities if the securities acquired are necessary to meet minimum requirements of local law, or are derived in the ordinary course of an underwriting, brokerage, or commercial banking business.

COMMENTS

Acquisitions made in connection with business transactions with a person in a foreign country should be exempt even though such person is not technically doing business in the foreign country.—National Association of Manufacturers

* * * * *

Acquisitions by an "investment bank" should be exempt in the same manner as acquisitions made by commercial banks. Moreover, the statutory prohibition should be against foreign corporations formed or availed of for the primary purpose of avoiding the interest equalization tax rather than being formed or availed of for the purpose of acquiring securities of a foreign corporation.—Baker, McKenzie & Hightower.

* * * * *

Exemption should apply to "dealers" rather than "brokers" since brokers do not acquire securities.—Investment Bankers Association of America.

Subsection (c) provides that the direct investment rule of subsection (a) does not apply if the 10-percent shareholder of the foreign corporation intends to sell the securities he acquires to U.S. persons.

NO COMMENTS

Section 4916. Exclusion for investments in less developed countries

Subsection (a), in general, provides that the tax shall not apply to the acquisition by U.S. persons of—

- (1) debt obligations of a less developed country; or
- (2) stock or debt obligations of less developed country corporations.

COMMENTS

In addition to the provision relating to investments in less developed country corporations, provision should be made to exclude investments made in a less developed country in an individual capacity or through a partnership, trust, etc.—National Association of Manufacturers.

* * * * *

Should exempt all investments or loans, whether or not with a corporation, made in any less developed country for activities within such countries.—Standard Oil Co. (New Jersey).

* * * * *

An exclusion should be provided for debt obligations of individuals and partnerships of a less developed country.—United Fruit Co.

* * * * *

Exemption should apply to obligations acquired from partnerships and other noncorporate organizations.—American Institute of Certified Public Accountants.

* * * * *

Exemption should apply to obligations of individuals and partnerships as well as to investments in holding companies.—United States Council of the International Chamber of Commerce, Inc.

Subsection (b) provides that the President of the United States shall designate which countries are to be treated as being less developed for purposes of the bill.

NO COMMENTS

Subsection (c) defines the term "less developed country corporation."

COMMENTS

Provision should be made to exempt investment in a company which holds the stock of various operating companies which themselves qualify as less developed country corporations. This amendment would make the definition of a less developed country corporation consistent with the definition used for foreign tax credit purposes.—Deltec Panamerica S.A.

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The definition of a less-developed country corporation used for foreign tax credit purposes should be used.—Liberian Iron Ore, Ltd.

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The definition of a less-developed country corporation used for foreign tax credit purposes should be used.—Association of the Bar of the City of New York.

* * * * *

A holding company for a less developed country corporation should qualify—American Institute of Certified Public Accountants.

* * * * *

In the case of new issues distributed before enactment of the bill, provision should be made to permit post acquisition approved by the Treasury Department of the issue as being an issue of a less developed country corporation—American Institute of Certified Public Accountants.

* * * * *

Income from sources within the United States, and assets located in the United States, should be treated as less developed country income, and assets, for purposes of determining qualification of a corporation as a less developed country corporation—American Institute of Certified Public Accountants.

Section 4917. Exclusion for New Issues Where Required for International Monetary Stability

This section permits the President of the United States to exempt from tax certain new issues of foreign securities. The exemption may be limited in dollar amount and/or for a specified period. If the exclusion is limited, it applies to those securities to which registration statements first become effective or to which notification first occurs.

COMMENTS

Exemption should be broadened to permit exemption statement with the Securities and Exchange Commission rather than on the time the registration statement becomes effective—Investment Bankers Association of America.

* * * * *

It would seem more equitable for the exemption to apply to those issues as to which registration statements or notifications were first filed.—Association of the Bar of the City of New York.

* * * * *

Exemption should be broadened to permit exemption from outstanding issues.—United States Council of the International Chamber of Commerce, Inc.

Section 4918. Exemption for Prior American Ownership

Subsection (a) provides that the tax shall not apply to a person who acquires a foreign security from a person who was a U.S. person throughout the period of his ownership of the security or continuous since July 18, 1963.

COMMENTS

Exemption should also apply in cases where a U.S. person sells securities after immigrating to the United States after July 18, 1963.—Kramer, Marx, Greenlee & Backus.

Subsection (b) provides that receipt of a certificate of American ownership shall be conclusive proof that the purchaser is exempt from tax unless the purchaser knew the certificate was false in a material respect.

COMMENTS

The use of blanket certificates of American ownership as proof of the purchaser's exemption from tax, presently authorized for national security exchange transactions, should be authorized with respect to over-the-counter transactions—Association of Stock Exchange Firms.

* * * * *

The procedure worked out by the Treasury Department and the New York Stock Exchange whereby no certificate of American ownership need accompany a certificate of stock traded on the exchange should be codified—New York Stock Exchange.

Section 4919. Sales by Underwriters and Dealers to Foreign Persons

Subsection (a) provides exemption from tax for—

(1) underwriters to the extent they sell foreign securities to non-U.S. persons in connection with private placements or public offerings registered with the Securities and Exchange Commission; and

(2) dealers in dollar bonds if the dollar bonds are sold to non-U.S. persons within 30 days after their acquisition.

COMMENTS

The requirement that an offering must be registered with the Securities and Exchange Commission in order to be exempt should be deleted since offerings of less than \$300,000 and offerings sold entirely to foreigners are exempt from registration—Cahill, Gordon, Reindel & Ohl.

* * * * *

Provision should be expanded to cover all public offerings regardless of whether registration is required—Association of the Bar of the City of New York.

Subsection (b) sets forth the general procedure to be followed by a person claiming an exemption as an underwriter or dealer.

NO COMMENTS

Subsection (c) defines the terms "underwriter," "dealer," and "foreign dollar bonds."

NO COMMENTS

Section 4920. Definitions

Paragraph (1), in general, defines the term "debt obligation" to include any indebtedness, whether or not in writing and whether or not bearing interest. It also includes any interest, option, or right in a debt obligation. The definition excludes convertible debentures, notes received as compensation for services, and obligations arising out of divorce.

COMMENTS

Convertible debentures should be taxed as debt obligations. A 15-percent tax should be paid upon conversion and a credit given at that time for the tax paid on the bond—Smith, Barney & Co.

* * * * *

The exclusion authorized for debt obligations received as compensation for services should be extended to exclude *stock* received as compensation for services rendered—National Constructors Association.

* * * * *

Exemption should be made for *stock* received as compensation—American Institute of Certified Public Accountants.

* * * * *

The bill should not apply to debt obligations received by a U.S. person as a result of services performed by a 50 percent-owned foreign subsidiary of the U.S. person—Chicago Bridge & Iron Co.

Paragraph (2) defines the term stock to include stock or shares of a corporation, the partnership interest of a limited partner, and option or rights to acquire stock.

NO COMMENTS

Paragraph (3) defines the term "foreign issuer or obligor." Subparagraph (A) of paragraph (3) sets forth the general rule that a foreign issuer or obligor includes—

- (i) an international organization of which the United States is not a member;
- (ii) a government of a foreign country; and
- (iii) foreign corporations, partnerships, trusts, estates, associations, insurance companies, or joint-stock companies.

NO COMMENTS

Subparagraph (B) of paragraph (3) treats as a foreign obligor any domestic corporation which is formed or availed of for the principal purpose of acquiring capital for a foreign person.

NO COMMENTS

Subparagraph (C) of paragraph (3) permits a domestic regulated investment company which has 80 percent of its assets in foreign securities to elect to be treated as a foreign corporation. Such a cor

poration may not, however, borrow or issue new stock after July 18, 1963, and before its election; except for issues registered with the Securities and Exchange Commission before July 18, 1963, and sold before September 15, 1963. Elections under this provision must be made within 30 days after enactment of this provision. The effective date of an election is to be determined by the electing corporation.

COMMENTS

A regulated investment company making an election under this provision should be permitted to make the election with respect to its investments retroactive to July 18, 1963; but, shares in the fund should not be treated as shares of a foreign corporation with respect to transfers by shareholders until after the date of enactment of the bill—Japan Fund, Inc.

* * * * *

Electing funds should be permitted to switch their foreign investments tax free during the period July 18, 1963, to the date of their election. Moreover, purchasers of stock in the fund should also be exempt from tax for this interim period. Failure to adopt this provision would be unfair and inequitable since purchasers of stock in a fund during the interim period might not have foreseen a retroactive election by the fund—Eurofund, Inc.

Paragraph (4) defines the term "United States person."

NO COMMENTS

Paragraph (5) defines the term "period remaining to maturity."

COMMENTS

Provision should be made to permit refund of a tax if a loan is prepaid—New York Clearing House.

* * * * *

The definition should be amended to exclude demand deposits, for example, demand deposits in a foreign bank—Connor, Winters, Randolph & Ballaine.

EFFECTIVE DATES

In General

The tax is, in general, applicable to acquisitions of foreign securities by U.S. persons after July 18, 1963.

COMMENTS

The bill should be made effective on the date of enactment—Association of Stock Exchange Firms.

Exemption for preexisting commitments

The bill does not apply to acquisitions made after July 18, 1963, pursuant to an obligation which on July 18, 1963 was—

1. unconditional; or
2. subject only to conditions contained in a formal contract under which partial performance had occurred.

COMMENTS

The bill should exempt contracts which on July 18, 1963, were subject only to the satisfaction of conditions which were not within the purchasers' control—Investment Bankers Association.

* * * * *

Acquisitions made after July 18, 1963, should be exempt if, prior to such date, the acquisition was subject to a firm purchase agreement or had reached a stage where none of the important terms or conditions were under the buyers' control. The buyer should be required to provide satisfactory evidence of the agreement and the stage of negotiations on July 18, 1963—Keystone Custodian Funds, Inc.

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The bill should exclude transactions which had progressed to the point where a memorandum of terms or a commitment letter had been exchanged prior to July 18, 1963—Henry J. Clay.

* * * * *

Exemption should be made for commitments evidenced by a commitment letter signed on or before July 18, 1963—Morgan Stanley & Co.

* * * * *

The bill should not apply to an obligation, understanding, or plan which was in existence on July 18, 1963, and under which partial performance or execution, such as obtaining foreign exchange control permits or organization of a foreign corporation, had occurred as of such date—Baker, McKenzie & Hightower.

* * * * *

Acquisitions made after July 18, 1963, should be exempt if the purchase, or commitment to purchase, had been formally approved before July 18, 1963, by a finance or investment committee of an insurance company, pension trust, educational or charitable institution, or similar institutional investor—Breed, Abbott & Morgan.

* * * * *

As a practical matter, life insurance companies consider themselves obligated to complete a transaction after reaching an understanding with the other party even though certain customary conditions remain to be fulfilled before the company is legally committed. Transactions in this state on July 18, 1963, should be exempt—American Life Convention and Life Insurance Association of America.

Exemption for public offerings registered with the Securities and Exchange Commission

The bill does not apply to acquisitions made on or before September 15, 1963 if—

1. a registration statement with respect to the security was in effect at the time of the acquisition,
2. the registration statement was filed with the Securities and Exchange Commission in the 90-day period prior to July 18, 1963; and
3. no material amendments to the registration statement had been filed after July 18, 1963.

COMMENTS

The exemption should be extended to the private placement of foreign securities in all cases where within 90 days prior to July 18, 1963, a placing banker had received firm authorization from a foreign issuer to proceed with the private placement on specified terms as to amount, maturity, and interest rate—R.W. Pressprich & Co.

* * * * *

The exemption should be amended to apply to acquisitions made on September 16, 1963, in order to conform the statute to public announcements made by the Treasury Department on July 18, 1963, relating to the effective date of the tax.—Cahill, Gordon, Reindel & Ohl.

Exemption for listed securities

The bill does not apply to acquisitions of foreign securities by a U.S. person if the foreign security was acquired on a national stock exchange before August 17, 1963.

NO COMMENTS

Exemptions for the exercise of options and the acquisition of securities as a result of foreclosure

The bill does not apply to acquisitions made pursuant to an option acquired before July 19, 1963, or to acquisitions made as a result of a foreclosure.

COMMENTS

The bill should also exclude stock acquired as a result of the exercise of an option by the estate, heir, or legatee of a person whose acquisition would not have resulted in tax.—Association of the Bar of the City of New York.

RETURN AND PENALTY REQUIREMENTS

The bill provides for—

1. Quarterly returns by persons incurring liability for tax and by persons who would be liable for tax except for the fact the security acquired carried with it a certificate of American ownership.

2. A civil penalty of the greater of \$10 or 5 percent of the amount of tax that would be due (but computed without regard to the exemptions for certificates of American ownership or sales to foreigners by underwriters, etc.) had a return been filed. The maximum penalty shall not exceed \$1,000.

3. A civil penalty of 125 percent of the tax that would otherwise have been paid by the purchaser if a person executes a false certificate of American ownership or certificate of sale to foreign persons. In addition, criminal penalties of \$1,000 and imprisonment for not more than 1 year may also be imposed for the willful execution of a fraudulent certificate.

NO COMMENTS

DENIAL OF DEDUCTION FOR TAX PAID

The bill, in general, denies a deduction for tax paid by a U.S. person in connection with the acquisition of a foreign security and provides that the tax shall be added to the basis of the security acquired. However, a deduction is allowable if the U.S. person is reimbursed for the tax by a foreign issuer or obligor and is required to include such reimbursement in income.

COMMENTS

Deduction for the tax should be allowed even though reimbursement is includible in income in a taxable year which differs from the one in which the tax was paid.—National Association of Manufacturers.

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Provision should be made in the case of original issue discount obligations to permit the tax to be treated as an additional price paid for the obligation. Provision should also be made to permit amortization of the tax over the period of the indebtedness.—Association of the Bar of the City of New York.

V. ALTERNATIVE PROPOSALS

Public witnesses recommended consideration of the following alternatives to enactment of H.R. 8000:

The solution to the U.S. balance-of-payments deficit position must be found in top-level political agreement among the leaders of the free world. Such agreement must define the mutual obligations of the parties with respect to the budgetary and foreign exchange costs of defending Europe and containing Communist China in the Far East.

Reduce non-asset-creating expenditures abroad.

Increase longer term interest rates.

Arrange a major drawing on the International Monetary Fund.

Remove the 25-percent gold cover on U.S. currency.

Issue special certificates and bonds denominated in currencies of foreign countries.

Establish a new international monetary mechanism with ability to expand credit to provide an effective means of financing world trade.

Seek voluntary restraints on the making of foreign investments by large institutional investors.

Create a capital issues committee to screen all foreign demands on the U.S. capital markets.

Adopt a program of tax incentives for persons who increase their export of U.S. manufactured goods.

Impose temporary direct restrictions on investments of American companies in industrial foreign countries.

Restrict or place a tax on foreign travel by U.S. persons.

Encourage investment in the United States by—

(a) reducing or eliminating the withholding tax on dividends and interest paid foreign investors; and

(b) increasing the estate tax exemption of nonresident aliens from \$2,000 to \$60,000.

Discourage foreign investment by U.S. persons through repeal of the foreign tax credit.

Require that tax-exempt organizations pay tax on their foreign source income.