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COMMITTEE PRINT

AMENDMENTS RECOMMENDED BY THE TREASURY DEPARTMENT

TO

H.R. 8000

INTEREST EQUALIZATION TAX ACT

COMMITTEE ON FINANCE
UNITED STATES SENATE

(THESE AMENDMENTS HAVE NOT BEEN CONSIDERED BY THE SENATE COMMITTEE ON FINANCE. THEY ARE BEING PRINTED FOR INFORMATIONAL PURPOSES ONLY)

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LETTER OF TRANSMITTAL

THE SECRETARY OF THE TREASURY,
Washington D.C., June 12, 1964.

Hon. HARRY FLOOD BYRD,
Chairman, Committee on Finance,
U.S. Senate, Washington, D.C.

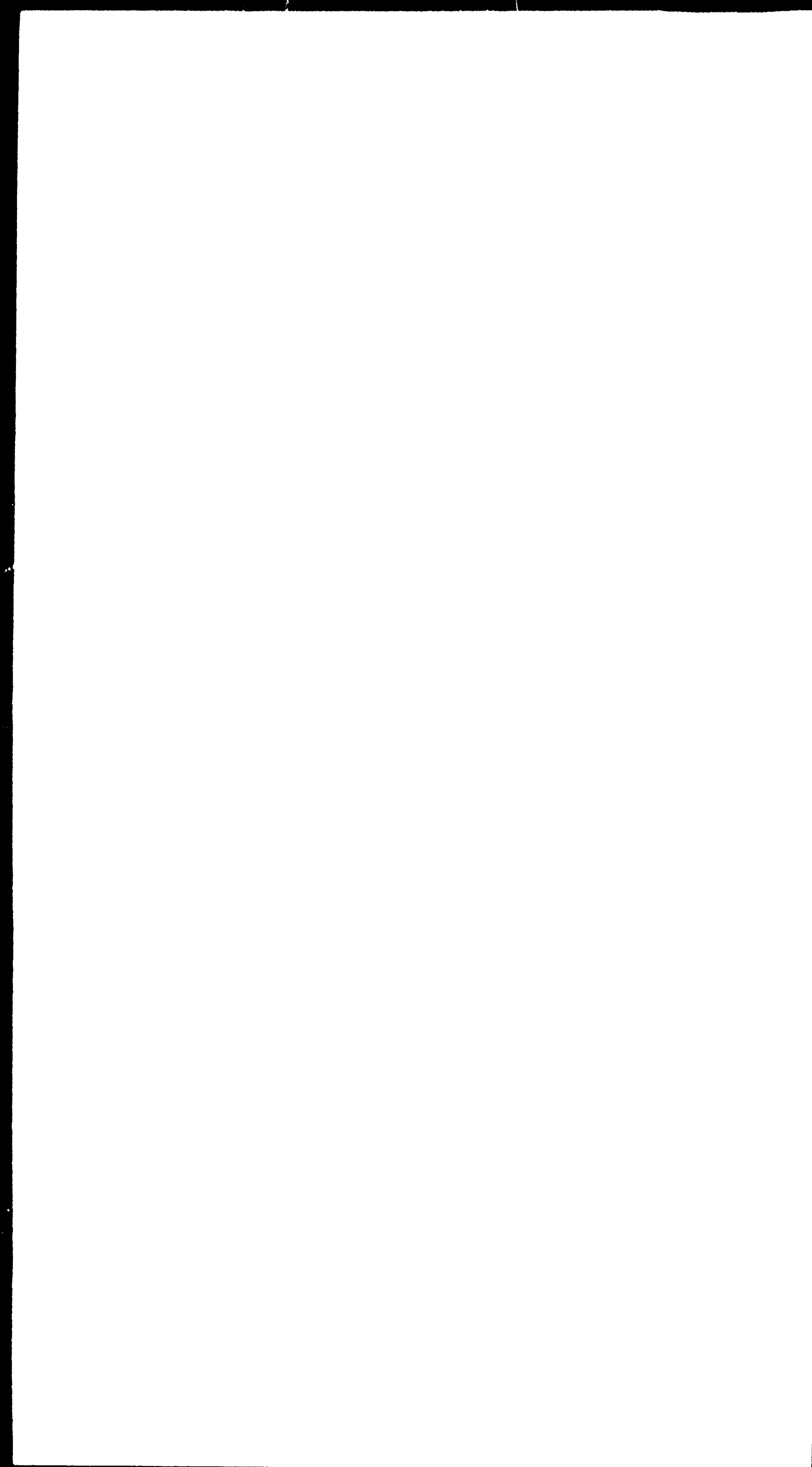
DEAR MR. CHAIRMAN: I am transmitting with this letter a series of proposed amendments recommended by the Treasury Department to the proposed interest equalization tax bill (H.R. 8000). This bill occupies a central position in our total effort to achieve prompt and lasting improvement in our balance of payments by reducing the flow of long-term portfolio capital from this country. The purposes of the bill are achieved through the imposition of a temporary excise tax on the acquisition from foreigners of foreign stocks or debt obligations with maturities of 3 years or more.

The proposed amendments are fully consistent with the principles of the bill as passed by the House. The changes embodied in these amendments are directed at technical problems which have been raised since House passage of H.R. 8000 and are designed for the most part to extend or clarify exclusions contained in the House bill, without at the same time weakening the effectiveness of the proposed legislation.

The Treasury Department believes it would be helpful to have these proposed amendments made public at this time by your committee. Publication of the amendments would enable interested persons to learn the Treasury's views on the various questions which have been brought to our attention since House passage of the legislation. This will permit them to focus on the proposed amendments in framing any comments they may wish to submit in connection with the bill.

Sincerely yours,

DOUGLAS DILLON.



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SUGGESTED AMENDMENTS TO THE INTEREST EQUALIZATION TAX BILL (H.R. 8000) PROPOSED BY THE TREASURY DEPARTMENT

GENERAL EXPLANATION

The Treasury Department recommends that the interest equalization tax bill (H.R. 8000) be amended in accordance with the proposed changes described in this statement. The bill is designed to relieve pressure on the balance of payments by bringing the cost of portfolio capital raised in the U.S. market by foreign persons more closely into alinement with the costs prevailing in markets in other industrial countries. This purpose would be achieved by imposing a temporary tax on acquisitions by Americans of certain foreign securities from foreigners. The suggested amendments are fully consistent with the intent of the bill as passed by the House and do not depart from the basic provisions and framework of that bill.

In general, the changes resolve technical problems which have been brought to the attention of the Treasury during the period since House passage of H.R. 8000. Some of the suggested amendments modify and extend certain exclusions so that the purposes of the bill may be achieved without unnecessarily impeding use of normal sources or techniques of financing. Other amendments simply clarify existing provisions and provide for more effective administration of the proposed tax.

EXPORT PROVISIONS

Amendments are being proposed to expand the export provisions of the bill, in order to give further assurance that the tax does not interfere with the legitimate export financing of U.S. goods and services. One proposed change extends the exclusion for stock and debt obligations arising from the sale of property produced in the United States to intangible property (such as patents and copyrights) as well as tangible property. A second proposed amendment liberalizes the rule permitting an exporter to transfer free of the tax a debt obligation received in the financing of U.S. exports. Another change makes clear that the exclusion provided by the bill where payment of an export loan is guaranteed or insured in whole or in part by the Export-Import Bank, remains available even if the loan gives rise to separate obligations.

The suggested amendments propose an extension of the exclusion contained in the bill for loans made in connection with the sale of ores or minerals extracted outside the United States. The categories of corporations which qualify as extractive companies would be broadened, and ores or minerals obtained under a contract entered into on or before July 18, 1963, would be covered by the provision. These changes recognize additional situations in which U.S. persons have a substantial economic interest in the extracted ore or mineral.

INSURANCE COMPANY PROVISIONS

A series of changes are suggested in the provisions dealing with insurance companies doing business in foreign countries so as to clarify those provisions and to perfect their technical application. Under the proposed amendments, insurance companies are permitted to include short-term obligations payable in foreign currency within their initial designation of exempt funds of assets of foreign securities, and to use the adjusted basis of the securities, rather than actual value, as the means of valuing the funds. The amendments require the companies to fill up their designated funds of exempt assets annually to the limit provided in the bill, to the extent of purchases made during the calendar year of stock and debt obligations otherwise excluded from tax under the new issue exclusion of section 4917 and the less-than-3-year exemption. The amendments also clarify the method of determining a company's allowable reserve for the year 1963, and permit insurance companies for purposes of determining the size of the designated funds to estimate the growth in their foreign business during a year. This will avoid the necessity of paying tax throughout the year on acquisitions in excess of the size of the fund at the end of the previous year, and claiming a credit or refund at the end of the year.

ADDITIONAL EXCLUSIONS

Amendments are being proposed which exclude certain types of acquisitions from tax. The proposed new exclusions include provisions relating to acquisitions of stock and debt obligations in lieu of payment of foreign tax; purchases of stock in order to obtain the right to occupy a dwelling; and acquisitions of obligations received in connection with the sale of a wholly owned foreign subsidiary. Acquisitions of these types are due to factors other than the relative return on capital between the United States and foreign countries. It is also proposed that the tax not apply to the acquisition of a debt obligation which is part of the purchase price of real property located in the United States, if the foreign buyer pays at least 25 percent of the purchase price to the American seller in U.S. dollars. Such a transaction has a favorable impact on the U.S. balance of payments and the exclusion is fully consistent with the purposes of the legislation.

DIRECT INVESTMENT

The changes in this section are designed to permit broader use of the direct investment exclusion. One change permits a U.S. corporation holding a 10-percent or more interest in a foreign corporation to acquire from the foreign corporation debt obligations which had previously been acquired by the foreign corporation in the ordinary course of its business as a result of the sale or rental of products manufactured or assembled by it or the performance of services by it. This form of financing is an alternative to a direct investment by the U.S. parent corporation in its foreign subsidiary. The suggested amendments also make available a credit or refund on purchases where a 10-percent or more interest is acquired over a 12-month period, whether or not the period coincides with a particular calendar year. In these situations, the credit or refund is made available with respect to debt obligations as well as stock.

LESS DEVELOPED COUNTRIES

The amendments propose that the less developed country provisions be expanded to permit the tax-free acquisition of stock and debt obligations by a U.S. person who is required to reinvest in a less developed country the payments received under a contract of sale (or indemnification) with the less developed country, resulting from the actual or threatened expropriation, nationalization, or seizure of the U.S. person's property in that country. Under such circumstances, the companies in which the U.S. person is required to invest presumably would qualify as less developed country corporations, but the conditions under which the investments are required to be made may make it impossible for the U.S. person to obtain the requisite proof.

Changes are also proposed in the provision defining a "less developed country corporation" to expand the number of companies which would qualify under the provision. The amendments are directed primarily at corporations doing business in less developed countries which may hold U.S. assets, obligations of individuals resident in less developed countries, or assets temporarily in foreign bank accounts (other than in less developed countries).

EXCLUSION FOR NEW ISSUES WHERE REQUIRED FOR INTERNATIONAL MONETARY STABILITY

One of the suggested amendments in this section clarifies the definition of what constitutes a new issue of debt obligations for purposes of this exclusion to make clear that construction loans are eligible to qualify. The other proposed change is designed to facilitate procedural operation of the exclusion by authorizing the President to extend the period of time within which an acquisition must be made after filing of the required notice.

SALES BY UNDERWRITERS AND DEALERS

One of the suggested amendments in the provisions of the bill dealing with transactions by underwriters and dealers permits a foreign underwriter participating in a public offering in the United States with American underwriters to elect to be treated as a U.S. person for purposes of his participation in the offering. This change will facilitate uniform pricing of the offering and eliminate return filing burdens for U.S. purchasers acquiring from the foreign underwriter.

The suggested amendments also permit a dealer to claim a credit or refund on the sale of debt obligations to foreigners within 90 days of purchase if the obligations are sold to another dealer who in turn sells to a foreigner on the date of purchase or the next business day. This change recognizes certain trading practices in the securities industry. The amendments also authorize the establishment of procedures by the stock exchanges and the over-the-counter market to provide a dealer with proof that the security was sold to a foreign person. Appropriate penalties are provided in the bill if these procedures are abused.

The proposed changes also permit a credit if a dealer acquires foreign stock in the ordinary course of his business and sells the stock on the

same business day to a foreigner. This proposal is designed to permit dealers to conduct certain types of arbitrage activities without at the same time weakening the effectiveness of the tax.

LIMITATIONS ON TAX

Three amendments are suggested in the section of the bill which limits the tax imposed on certain acquisitions so as to expand the situations in which the special rules limiting application of the tax may be utilized. The first of these permits an American who acquires a debt obligation from another American (free of the tax) and who later exercises the right to convert the debt obligation into stock to offset against his liability the amount of tax which would have been imposed if the obligation had been acquired in a taxable transaction. The bill now permits an offset only with respect to tax which was actually paid on acquisition of the obligation. A second change permits an American, exercising a subscription right to acquire stock or a debt obligation within 90 days from the date of the distribution of the rights, to use the exercise price as his tax base, whether or not he was the original distributee of the rights. The bill presently limits use of the exercise price to the original recipient of the rights from the issuer. The third amendment avoids the possibility of a double tax where a domestic corporation has been formed or availed of for the benefit of a foreign borrower.

PREEXISTING COMMITMENTS

The suggested amendments propose a liberalization of the provisions in the bill exempting certain transactions from the generally effective date of the tax of July 19, 1963, because of the existence of a preexisting commitment. They extend the exemption to situations where application of the tax might involve hardship to the parties because of the advanced state of negotiations on July 18, 1963. An exemption is also provided if the acquisition was pursuant to a contract of sale to a less developed country entered into on or before July 18, 1963, if the contract requires reinvestment of the proceeds in that country.

ORIGINAL ISSUE DISCOUNT

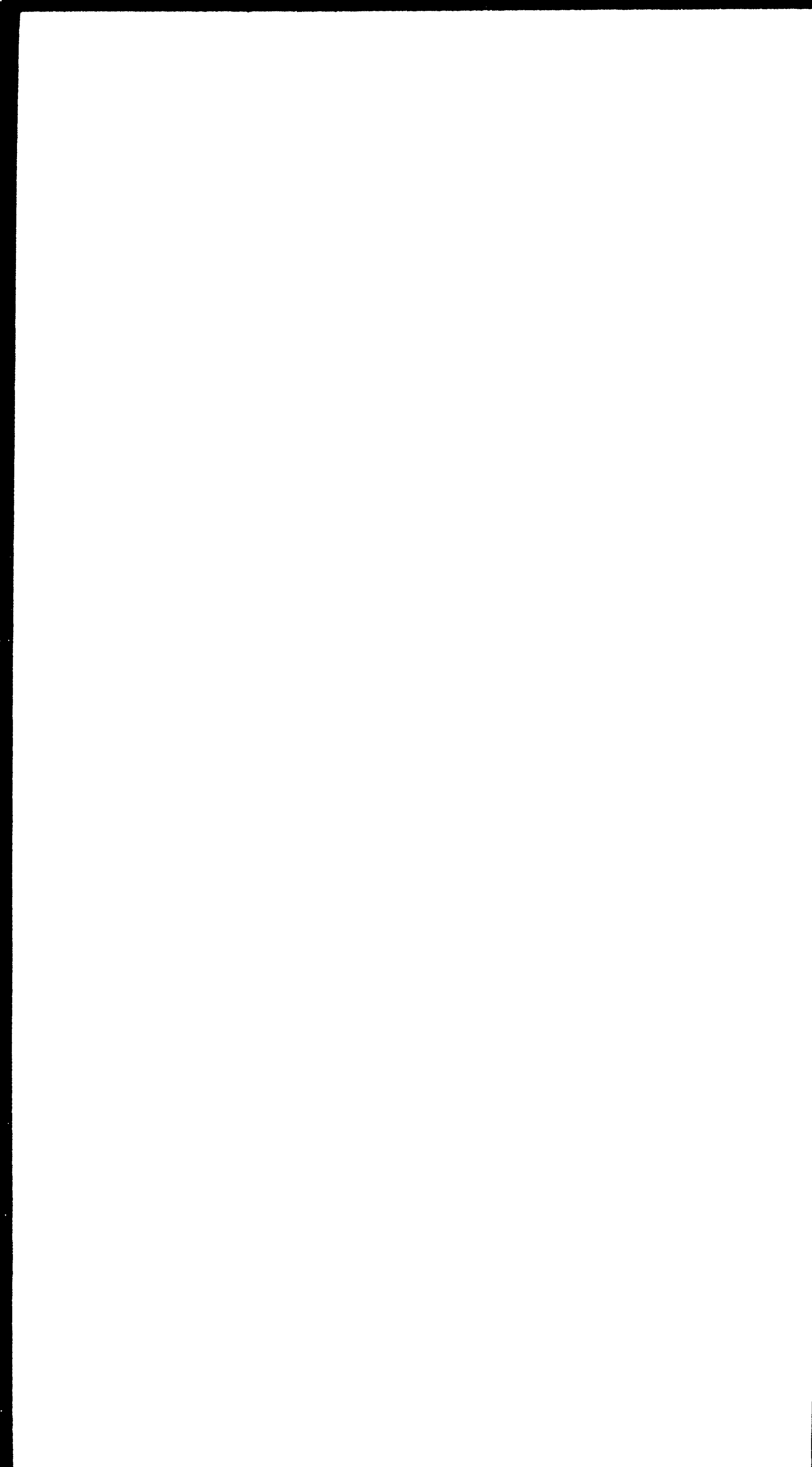
The proposed amendments suggest a change in the provisions of the Internal Revenue Code dealing with the taxation of the difference between the issue price of bonds and the stated redemption price at maturity of such bonds, i.e., "original issue discount." The amendment is designed to prevent the interest equalization tax from creating adverse income tax consequences in the case of private placements of bonds.

ADMINISTRATIVE PROVISIONS

The proposed amendments provide that proof of the exemption for prior American ownership must be in the form of a certificate of American ownership or a confirmation received from a member of a registered exchange or the National Association of Securities Dealers, unless reasonable cause is submitted for the inability to produce such evidence. This technical change is needed because of other pro-

visions already contained in the bill which are designed to facilitate trading in foreign securities. In the overwhelming majority of purchases of foreign securities, a confirmation will be received by the American buyer which satisfies the requirements of the bill, and no return or filing is necessary. However, if no confirmation or certificate is obtained or submitted, a person claiming the exemption for prior American ownership must file a statement explaining his inability to submit the certificate, together with a summary of the evidence establishing the exemption.

A second proposed administrative change relates to required recordkeeping and information filing by members of stock exchanges and the National Association of Securities Dealers. The present bill requires recordkeeping and the filing of information by the seller's broker in transactions where the exemption for prior American ownership is claimed, since the action of the seller's broker in accepting a certificate of American ownership results in no tax being due from the purchaser. The suggested amendments apply recordkeeping and filing requirements to transactions in which no exemption is available (and tax is due), since such records and information are essential to facilitate enforcement of the tax.



PROPOSED AMENDMENTS AND TECHNICAL EXPLANATION

Section 4913. LIMITATION ON TAX ON CERTAIN ACQUISITIONS

(a) CERTAIN SURRENDERS, EXTENSIONS, RENEWALS, AND EXERCISES. Page 7, line 7.

(3) SPECIAL LIMITATIONS. Page 8, line 19.

(A) CONVERSIONS OF DEBT OBLIGATIONS INTO STOCK. Page 8, line 20.

This subparagraph should be amended to read as follows:

"The tax imposed upon an acquisition of stock pursuant to the exercise of a right to convert a debt obligation (as defined in section 4920(a)(1)) into stock shall be limited to—

"(i) the amount of tax which would have been imposed by section 4911 if the debt obligation [pursuant to section 4920(a)(2)(D),] had been treated as stock at the time of its acquisition by the person exercising the right (or by a decedent from whom such person acquired the right by bequest or inheritance or by reason of such decedent's death), less

"(ii) the amount of tax paid by the person exercising the right (or by such decedent) as a result of the acquisition of the convertible debt obligation *or, if such acquisition was not subject to the tax imposed by section 4911, the amount of tax which would have been imposed as a result of such acquisition if such acquisition had been subject to such tax.*

The proposed change is designed to provide consistent treatment in the bill on the exercise of rights to convert foreign debt obligations acquired by Americans from other Americans, and to facilitate trading in these securities among Americans.

Section 4912 (a) of the bill provides that the exercise of the right to convert a foreign debt obligation which is convertible for at least 5 years after interest begins to accrue is a taxable acquisition of stock by the person exercising the right. The revised subparagraph will permit a U.S. holder of such convertibles to offset against the tax liability arising on conversion any tax which would have been payable if the convertible obligations had been acquired in a transaction subject to the tax, regardless of whether such a tax was actually paid. The proposed change removes the distinction which would allow a credit to U.S. persons acquiring foreign convertibles directly from the foreign issuer in a private placement, but would deny the credit to a purchaser in a public offering, who acquires from the U.S. underwriter and not directly from the foreign issuer. The amendment will make the credit available to both.

(B) EXERCISE OF CERTAIN SHAREHOLDERS' RIGHTS. Page 9, line 12.

This subparagraph should be amended to read as follows:

"The tax imposed upon an acquisition of stock or a debt obligation of a foreign corporation by a United States person [who is a shareholder of such corporation], where—

"(i) the stock or debt obligation is acquired pursuant to the exercise of an option or similar right to acquire such stock or debt obligation which was acquired [by such person] *by a shareholder of such corporation* in a distribution [by such corporation] with respect to to its stock, and

"(ii) such option or right [by its terms expires or terminates within a period not exceeding 90 days from the date so distributed to him] *is exercised within 90 days from the date of its distribution by such corporation*

shall be limited to the amount of tax which would have been imposed by section 4911 if the price paid under such option or right were the actual value of the stock or debt obligation acquired.

The proposed changes are designed to extend the benefit of using the exercise price as the tax base to subsequent holders of subscription rights as well as shareholders, and to permit this limitation to be used where exercise occurs within 90 days of the distribution, regardless of any ambiguity in the terms of the offering which might make it unclear whether the rights offering actually terminated within 90 days of issuance.

The balance-of-payments outflow in the case of the exercise of subscription rights is no greater than the exercise price, whether the rights are exercised by the original recipient or a subsequent purchaser. The proposed extension of the use of exercise price as the tax base for subsequent purchasers is thus consistent with the purposes of the bill, and removes a possible impediment to the market in such rights.

"(c) *Acquisitions by Certain Domestic Corporations and Partnerships*. Following page 11, line 3.

This new subsection should provide as follows:

"If stock or a debt obligation of a foreign issuer or obligor is acquired by a domestic corporation or a domestic partnership with funds obtained as the result of an acquisition by a United States person of stock or a debt obligation of such corporation or partnership which under section 4912(b)(3) is deemed an acquisition by such person of stock or a debt obligation of a foreign issuer or obligor, the tax imposed upon the acquisition by the domestic corporation or the domestic partnership shall be limited to—

"(1) the amount of tax imposed by section 4911, less

"(2) the amount of tax paid by the United States person from whom the funds were obtained on the acquisition by such person which under section 4912(b)(3) is deemed an

acquisition of stock or a debt obligation of a foreign issuer or obligor.

This proposed subsection is designed to prevent the imposition of a double tax on the same transaction, where a foreign borrower has made use of a domestic corporation or partnership as a conduit to acquire funds from a U.S. lender.

Under section 4912(b)(3) of the bill, the legal entities of domestic corporations and partnerships which are formed or availed of for the principal purpose of channeling funds to foreign borrowers are disregarded with respect to such transactions, and the U.S. lender is taxed as if he were acquiring the stock or debt obligation directly from the foreign issuer or obligor. The present bill could also be construed to require a second tax to be imposed when the domestic entity passes the same funds along to the foreign corporation or partnership in exchange for the latter's debt obligation (or stock). Such a double tax goes beyond the necessary scope of the bill, and the proposed amendment will eliminate the possibility of that result.

Section 4914. EXCLUSION FOR CERTAIN ACQUISITIONS

(b) EXCLUDED ACQUISITIONS. Page 12, line 18.

"(*4*) *Acquisitions in lieu of payment of foreign tax.* Following page 14, line 4.

This is a new paragraph of subsection (b); present paragraph (4) should be renumbered (6).

> *"Of stock or debt obligations by a United States person doing business in a foreign country, to the extent such acquisition is made, in conformity with the laws of such foreign country, as a substitute for the payment of tax to such foreign country.*

This new provision excludes from tax the acquisition of foreign securities if such securities are purchased in lieu of the payment by a United States person doing business in a foreign country of tax imposed by that country. Certain foreign countries permit taxpayers to acquire foreign securities, generally housing bonds, instead of paying certain taxes imposed by the country. This paragraph recognizes that such a purchase should not be subject to the interest equalization tax since such an acquisition is not made in response to any interest rate differential between the United States and the foreign country.

"(*5*) *Acquisitions of stock in cooperative housing corporations.* Following page 14, line 4.

This is a new paragraph (5) of subsection (b).

> *"Of stock of a foreign corporation which entitles the holder, solely by reason of his ownership of such stock, to occupy for dwelling purposes a house, or an apartment in a building, owned or leased by such corporation.*

This proposed exclusion is designed to permit a U.S. person to acquire stock in a foreign corporation for the purpose of obtaining the right to occupy a house, or an apartment in a building, owned or leased by the corporation. Under the bill as presently drafted such an acquisition would be subject to the tax unless the U.S. person acquired a 10 percent or more interest in the foreign corporation. On the other hand, the tax is not applicable to the rental of an apartment by an

American living abroad, or to the purchase of a house abroad. The proposed change provides equivalent treatment to stock in cooperative housing corporations. The acquisition of stock in a corporation for the purpose of obtaining a dwelling would normally not be motivated by an interest rate differential between the United States and foreign countries.

(c) EXPORT CREDIT, ETC., TRANSACTIONS. Page 15, line 1.

(1) IN GENERAL. Page 15, line 2.

This paragraph should be amended as follows:

> "The tax imposed by section 4911 shall not apply to the acquisition from a foreign obligor of a debt obligation arising out of the sale of tangible personal property or services (or both) to such obligor by any United States person, if—
>
> "(A) payment of such debt obligation (*or of any related debt obligation arising out of such sale*) is guaranteed or insured, in whole or in part, by an agency or wholly-owned instrumentality of the United States; or
>
> "(B) * * *.

This proposed change makes clear that if payment of part of a loan is guaranteed or insured by an agency or wholly owned instrumentality of the United States, such as the Export-Import Bank, that portion of the loan which is not guaranteed or insured is excluded from the tax. This is true even if separate debt obligations are given for the guaranteed and nonguaranteed portions of the loan. This exclusion is based on the fact that the Export-Import Bank guarantees or insures a portion of a loan only if the entire loan is attributable to the sale of goods produced in the United States.

(3) *Certain interests in intangible personal property.* Following page 16, line 20. This is a new paragraph. Present paragraph (3) should be renumbered (4).

This new paragraph should read as follows:

> *"The tax imposed by section 4911 shall not apply to the acquisition by a United States person from a foreign issuer or obligor of its stock in payment for, or of a debt obligation arising out of, the sale to such issuer or obligor of—*
>
> *"(A) any interest in patents, inventions, models or designs (whether or not patented), copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, or other like property (or any combination thereof), or*
>
> *"(B) any such interest together with services to be performed, in connection with any such interest sold, by such United States person (or by one or more includible corporations in an affiliated group, as defined in section 1504, of which such person is a member),*
>
> *if not less than 85 percent of the purchase price is attributable to the sale of any interest in property described in subparagraph (A) which was produced, created, or developed in the United States by such United States person (or by one or more such includible corporations), or is attrib-*

utable to the sale of any interest in such property so produced, created, or developed and to the performance of services described in subparagraph (B).

This new provision is designed to provide a U.S. person who is selling intangible property, such as know-how, patents, and copyrights, treatment consistent with that already accorded to exporters of tangible property. Frequently, the sale of intangible property involves the acquisition by the selling U.S. person of a 10-percent interest in the foreign purchaser, which would be excluded from tax as a direct investment. However, there are situations where a 10-percent interest may not be acquired, particularly where the seller is a small U.S. company selling to a large foreign corporation. This new provision would permit a U.S. seller of intangible property to receive stock or debt obligations in connection with the sale of property which he produced, created, or developed, or in connection with the furnishing of services related to the sale of such property.

"(5) OTHER LOANS RELATED TO SALES BY UNITED STATES PERSONS. Page 17, line 14.

This paragraph should be amended as follows:

"The tax imposed by section 4911 shall not apply to the acquisition from a foreign obligor by a United States person of a debt obligation of such obligor if such debt obligation—

"(A) was received by such United States person as all or part of the purchase price provided in a contract under which the foreign obligor agrees to purchase for a period of 3 years or more ores or minerals (or derivatives thereof)—

(*i*) extracted outside the United States [(i)] by such United States person [(ii)] *or* by one or more includible corporations in an affiliated group (as defined in section 48(c)(3)(C)) of which such United States person is a member,

(ii) extracted outside the United States by a corporation at least 10 percent of the total combined voting power of all classes of stock of which is owned, directly or indirectly, by such United States person, by one or more such includible corporations, or by domestic corporations which own, directly or indirectly, at least 50 percent of the total combined voting power of all classes of stock of such United States person, or

(iii) obtained under a contract entered into on or before July 18, 1963, by such United States person, by one or more such includible corporations, or by such domestic corporations; or

[(iii) by a corporation at least 10 percent of the total combined voting power of all classes of stock of which is owned by such United States person, if at least 50 percent of such voting power is owned by United States persons each of whom owns at least 10 percent of such voting power; or]

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"(B) arises out of a loan (made by such United States person to such foreign obligor) the proceeds of which will be used by such obligor for the installation, maintenance, or improvement of facilities outside the United States which (during the period the loan is outstanding) will be used for the storage, handling, transportation, processing, or servicing of ores or minerals (or derivatives thereof) a substantial portion of which is extracted outside the United States by such United States person or by a corporation referred to in clause [(ii) or (iii)] *(i) or (ii)* of subparagraph (A) *or is obtained under a contract described in clause (iii) of subparagraph (A).*

This proposed change expands the exemption for ores and minerals extracted and sold outside the United States to include the sale of those ores and minerals in which the U.S. person has a substantial economic interest.

This change would permit an exclusion if the ores or minerals being sold by the U.S. person under a long-term sales contract are extracted outside the United States by the U.S. person acquiring the debt obligation, an affiliated company, or by a corporation in which the U.S. person, domestic corporations owning at least 50 percent of the voting stock of the U.S. person, or an affiliated company holds a direct investment (10 percent of the total voting stock), whether or not U.S. persons own 50 percent of the total voting stock of the foreign corporation. The proposed change also qualifies ores or minerals obtained under a contract entered into on or before July 18, 1963, by such U.S. person, domestic corporations, or an affiliated company, whether or not the extraction is performed by them. The bill also permits U.S. persons to acquire debt obligations of foreign obligors tax free if the proceeds of the loan are to be used by the borrower to install, maintain, or improve facilities for the storage, handling, transportation, processing, or servicing of ores or minerals extracted outside the United States which qualify under the proposed standards.

(e) ACQUISITIONS BY INSURANCE COMPANIES DOING BUSINESS IN FOREIGN COUNTRIES. Page 21, line 6.

(1) IN GENERAL. Page 21, line 8.

This paragraph should be amended as follows:

"The tax imposed by section 4911 shall not apply to the acquisition of stock or a debt obligation by a United States person which is an insurance company subject to taxation under section 802, 821, or 831, if [(A)] such stock or debt obligation is designated (in accordance with paragraph (3)) as part of a fund of assets established and maintained by such insurance company (in accordance with paragraph (2)) with respect to foreign risks insured or reinsured by such company under contracts (including annuity contracts) [which, by their terms, provide that the proceeds shall be payable] *the proceeds of which are payable* only in the currency of a foreign country[, and (B) the actual value of all of the assets held in such fund immediately after the stock or debt obligation has been designated as a part thereof does not exceed 110 percent

of the applicable allowable reserve determined in accordance with paragraph (4)]. As used in this subsection, the term "foreign risks" means risks in connection with property outside, or liability arising out of activity outside, or in connection with the lives or health of residents of countries other than, the United States.

The first change in the above provision is designed to make clear that an insurance contract qualifies as a policy insuring a foreign risk if the company is obligated to make payment in a foreign currency, whether the obligation to make such payment is stated in the policy itself or is required under the law of the applicable foreign jurisdiction. The second change eliminates a provision the substance of which is found elsewhere in the subsection (pars. (3)(A)(i) and (3)(E)(i)).

(3) DESIGNATION OF ASSETS. Page 23, line 8.

(A) INITIAL DESIGNATION. Page 23, line 9.

This subparagraph should be amended as follows:

"(i) REQUIREMENT OF INITIAL DESIGNATION.—An insurance company desiring to establish a fund (or funds) of assets under paragraph (2) shall initially designate, as part or all of such fund (or funds), stock *and debt obligations owned by it on July 18, 1963, as follows: First, stock of foreign issuers, and debt obligations of foreign obligors having a period remaining to maturity (on July 18, 1963) of 3 years or more and payable in foreign currency: second, if the company so elects, debt obligations of foreign obligors having a period remaining to maturity (on July 18, 1963) of less than 3 years and payable in foreign currency: and third, debt obligations of foreign obligors having a period remaining to maturity (on July 18, 1963) of 3 years or more and payable solely in United States currency. The designation under the preceding sentence with respect to any fund shall be made, in the order set forth, to the extent that the adjusted basis (within the meaning of section 1011) of the designated stock and debt obligations was (on July 18, 1963) not in excess of 110 percent of the allowable reserve applicable to such fund (determined in accordance with paragraph (4)(B)(ii)), and shall in no case include any stock or debt obligation described in section 4916(a).* [of foreign issuers, or debt obligations of foreign obligors having a period remaining to maturity of 3 years or more, or both, which it owned on December 10, 1963, to the extent that such stock or debt obligations or both had an actual value as of such date not in excess (in the case of any such fund) of 110 percent of the applicable allowable reserve of such com-

pany as determined in accordance with paragraph (4)(A). The designation or designations which an insurance company is required to make shall be made first from stock and debt obligations which were acquired by such company on or before July 18, 1963, and shall in no case include any stock or debt obligations described in paragraph (1), (2), or (3) of section 4916(a).]

"(*ii*) TIME AND MANNER OF INITIAL DESIGNATION.—Any initial designation which an insurance company is required to make under this subparagraph shall be made on or before the 30th day after the date of the enactment of this chapter (or at such later time as the Secretary or his delegate may by regulations prescribe) by the segregation on the books of such company of the stock or debt obligations (or both) designated.

This revised subparagraph is designed to give insurance companies doing business in foreign countries a different method of establishing their funds of assets. Under the method presently provided in the bill, insurance companies cannot designate debt obligations as part of the fund as an initial designation unless the obligations were owned on both July 18 and December 10, 1963. This means that an obligation which was held on July 18, 1963, and which matured before December 10, 1963, could not be designated as part of the fund. Moreover, debt obligations with less than 3 years remaining to maturity cannot be initially designated. This prevents obligations of less than 3 years maturity payable in foreign currency from being the subject of an initial designation, despite the fact that they may be attributable to the foreign business carried on by the insurance company. These short-term obligations may have originally been purchased as long-term obligations or as short-term obligations with the intention by the insurance company of reinvestment in long-term obligations payable in foreign currency. If these short-term obligations payable in foreign currency cannot be designated as part of the fund before long-term obligations payable in U.S. currency, the insurance companies would be unable to replace tax free those short-term obligations which are attributable to their foreign operations.

The proposed subparagraph provides an alternative method of establishing the fund of assets. The order of designation is as follows: (1) Stock and long-term debt obligations payable in foreign currency; (2) at the election of the company, short-term obligations payable in foreign currency; and (3) long-term debt obligations payable in U.S. currency. Ownership on December 10, 1963, is not required, since inclusion of this date is not necessary for effective operation of this provision as amended.

This subparagraph also includes a change directed at the valuation of assets in the fund. Under the present provision in the bill, an insurance company would be required to ascertain the fair market value of its fund of assets, including appraisals of mortgages and private placements, at the time of each new acquisition of stock or debt obligations, to determine if the new acquisition could be designated as part

of the fund without exceeding the fund's 110-percent limit. In order to eliminate the necessity of frequent revaluations of the fund's assets and to simplify Government audit procedures, the proposed change permits valuation of the fund of assets in terms of the adjusted basis of the securities held. This is also the value used for purposes of determining gain on sale or other disposition of securities under the applicable provisions of the Internal Revenue Code relating to income tax treatment of insurance companies.

(*B*) *CURRENT DESIGNATIONS TO MAINTAIN FUND.* Page 24, line 17.

This subparagraph should be amended as follows:

> "To the extent permitted by subparagraph [(C)] *(E), stock of a foreign issuer or a debt obligation of a foreign obligor acquired by an insurance company after July 18, 1963, may be designated as part of a fund of assets described in paragraph (2), if such designation is made before the expiration of 30 days after the date of such acquisition and the company continues to own the stock or debt obligation until the time the designation is made;* [an insurance company may claim an exclusion under this subsection with respect to the acquisition of stock or a debt obligation of a foreign issuer or obligor after Decem-10, 1963, if such company designates such stock or debt obligation as part of a fund of assets described in paragraph (2) before the expiration of 30 days after the date of such acquisition (and continues to own it until the time the designation is made);] except that any such stock or debt obligation acquired before the initial designation of assets to the fund is actually made as provided in subparagraph (A)(ii) may be designated under this subparagraph at the time of such initial designation without regard to such 30-day period and continued ownership requirements.

The changes in this subparagraph are intended to conform the provision with the amendments proposed in subparagraph (A).

(*C*) *Additional designations after close of year.* Page 25, line 9.

This is a new subparagraph (C); present subparagraph (C) is deleted.

> *"If the adjusted basis of the assets held in a fund of assets described in paragraph (2) at the close of a calendar year after 1963 is less than 110 percent of the allowable reserve applicable to such fund at the close of such year, the insurance company may, to the extent permitted by subparagraph (E), designate additional stock or debt obligations (or both) which were acquired during such calendar year as a part of such fund, so long as the company still owns such stock or debt obligations at the time of designation. Any designation under this subparagraph shall be made on or before January 31 following the close of the calendar year.*

> *Any tax paid by such company under section 4911 on the acquisition of the additional stock or debt obligations so designated shall constitute an overpayment of tax; and, under regulations prescribed by the Secretary or his delegate, credit or refund (without interest) shall be allowed or made with respect to such overpayment.*

This new subparagraph embodies the procedure now contained in paragraph (4)(B) of this subsection. This procedure permits an insurance company to designate stock and debt obligations as part of a fund of assets if the securities were acquired during the calendar year (and are held at the end of the year) and if the adjusted basis of the assets in the fund at the end of the year is less than 110 percent of the allowable reserve applicable to the fund. The securities may be designated up to the 110-percent limit. A credit or refund is available as to any tax which was paid on stocks or debt obligations which are so designated.

(D) Supplemental required designations.

This is a new subparagraph (D) following new subparagraph (C) added following line 8 on page 25.

> *If during any calendar year an insurance company acquires stock or debt obligations which are excluded from the tax imposed by section 4911 under an Executive order described in section 4917, and if at the close of the calendar year (and after the designation of additional assets under subparagraph (C)) the adjusted basis of all assets in a fund described in paragraph (2) is less than 110 percent of the allowable reserve applicable to such fund, such company shall, to the extent permitted by subparagraph (E), designate as part of such fund stock and debt obligations acquired by it during the calendar year and owned by it at the close of the calendar year, as follows: First, stock, and debt obligations having a period remaining to maturity (on the date of acquisition) of 3 years or more and payable in foreign currency, which were excluded from the tax imposed by section 4911 under such Executive order; second, if the company so e[illegible], debt obligations of foreign obligors having a period remaining to maturity (on the date of acquisition) of less than 3 years and payable in foreign currency; and third, debt obligations having a period remaining to maturity (on the date of acquisition) of 3 years or more and payable solely in United States currency, which were excluded from the tax imposed by section 4911 under such Executive order. The designations under this subparagraph shall be made on or before January 31 following the close of the calendar year.*

This new subparagraph establishes an ordering process for designating securities at the close of a calendar year if the fund of assets is not up to its 110-percent limit. The purpose of this provision is to prevent creation of a gap in the fund of assets which could defeat the

purposes underlying the imposition of a limit on the proposed exclusion for new issues provided in section 4917, if it were found necessary to impose such a limit. This gap could develop while the new issue exclusion was unlimited, if the insurance companies were not required to designate as part of the fund those securities which were excluded from tax under this new issue exclusion. If the President at a later time found it necessary to impose a limitation on this exclusion, insurance companies would then have room in their funds of assets to continue to buy new issues at a substantial rate. The proposed change prevents this result by requiring the designation at the end of the calendar year (if the fund is not full) of stock and long-term debt obligations (payable in foreign currency) which were originally excluded from tax during the calendar year under the new issue exemption; short-term debt obligations (payable in foreign currency), at the election of the company; and long-term debt obligations (payable in U.S. currency) which were originally excluded from tax during the calendar year under the new issue exemption.

(*E*) *Limitations.* Following new subparagraphs (C) and (D) added following line 8 on page 25.

This is a new subparagraph (E).

> "(*i*) *In general.—No designation of stock or a debt obligation as a part of a fund of assets described in paragraph (2) shall be made under subparagraph (B), (C), or (D), to the extent that, immediately thereafter, the adjusted basis of all the assets held in such fund would exceed 110 percent of the applicable allowable reserve (determined in accordance with paragraph (4)(B)(i)).*
>
> "(*ii*) *Treatment of excess designations.—To the extent that the adjusted basis of any stock or debt obligation designated as a part of a fund under subparagraph (B) during any calendar year, when added to the adjusted basis of all other assets held in such fund at the close of such calendar year, exceeds 110 percent of the allowable reserve applicable to such fund for such calendar year, the designation of such stock or debt obligation shall, for purposes of this subsection, be treated as ineffective, and the provisions of this chapter shall apply with respect to the acquisition of such stock or debt obligation as if such designation had not been made.*
>
> "(*iii*) *Short-term obligations.—No designation may be made under subparagraph (B) or (C) of any debt obligation which has a period remaining to maturity (on the date acquired) of less than 3 years.*

Clause (i) of this subparagraph states the general principle that no designation of stock or debt obligations may be made if the designation causes the adjusted basis of the assets in the fund to exceed 110 percent of the allowable reserve applicable to the fund. A comparable provision now appears in the bill as (3)(C).

Clause (ii) of this subparagraph permits an insurance company to estimate the increase in its allowable reserve during a particular

calendar year. As the bill is presently drafted, an insurance company whose fund of assets is completely filled must pay the tax on acquisitions even though its foreign business may increase during the calendar year so as to permit designation of the securities at the end of the year. Under present procedure, the company is required to pay the tax, and at the end of the year, apply for a credit or refund based upon the actual increase in its reserve. The proposed change permits a company to designate securities as part of a fund of assets based upon its estimate of the allowable reserve applicable to the fund at the end of the year. If the adjusted basis of the stock or debt obligations designated as part of the fund during the year, together with all other assets held in the fund at the end of the year, is less than 110 percent of the allowable reserve applicable to the fund, no tax is due. If, however, the adjusted basis of these assets exceeds 110 percent, designations in excess of that figure are treated as ineffective, and the company must pay the tax plus any interest which may be due on the acquisitions which were the subject of ineffective designations.

Clause (iii) of this subparagraph is designed to prohibit maintenance designations of short-term obligations during the calendar year. The acquisition of these obligations is not subject to the tax, and such maintenance designations could be utilized by insurance companies as a method of avoiding the impact of a limitation which might be placed on the exclusion provided in section 4917 for issues orginating in a country where application of the tax to that country imperils or threatens to imperil the stability of the international monetary system (new issue exclusion). In anticipation of the establishment of such a limit, insurance companies could fill their funds with short-term obligations and, after a limit were imposed, replace them with new long-term obligations tax free. This would have the effect of frustrating the purposes of the limit. Under proposed subparagraph (D), at the close of the calendar year, short-term obligations may be designated *after* new long-term obligations payable in foreign currency which were excluded from tax under section 4917.

(4) DETERMINATION OF RESERVES. Page 25, line 16.

This paragraph should be amended as follows:

> "(A) GENERAL RULE.—For purposes of this subsection, the term 'allowable reserve' means—
>
> "(i) in the case of a life insurance company (as defined in section 801(a)), the items taken into account under section 810(c) arising out of contracts of insurance and reinsurance (including annuity contracts) which relate to foreign risks and the proceeds of which are payable in a single foreign currency (other than the currency of a less developed country); and
>
> "(ii) in the case of an insurance company other than a life insurance company (as so defined), the amount of its unearned premiums (*under section 832(b)(4)*) and unpaid losses (*under section 832(b)(5)*) which relate to foreign risks insured or reinsured under contracts providing for payment in foreign currencies (other than currencies of less developed countries)

and which are taken into account in computing taxable income under section 832[(b)(4) and (5)] (for such purpose treating underwriting income of an insurance company subject to taxation under section 821 as taxable income under section 832).

[The determination of an allowable reserve of an insurance company for any calendar year shall be made as of the close of the previous calendar year.]

"(B) *TIME OF DETERMINATION.*—

"(i) *IN GENERAL.—For purposes of paragraph (3) (other than subparagraph (A) of such paragraph), the determination of an allowable reserve for any calendar year shall be made as of the close of such year.*

"(ii) *INITIAL DESIGNATION.—For purposes of paragraph (3)(A), the determination of an allowable reserve shall be made as of July 18, 1963. If the insurance company so elects, the determination under this clause may be made by computing the mean of the allowable reserve at the beginning and at the close of the calendar year 1963.*

Present subparagraph (B) is deleted.

The changes proposed in subparagraphs (A) and (B)(i) of this paragraph make clear that the determination of an allowable reserve for a fund of assets for any calendar year shall be made at the end of that year. Under the present bill, the reserve as of the close of the previous calendar year is used, although the company may elect to use the figure as of the close of the current year. This change recognizes that the reserve figure which should govern is the figure at the end of the current calendar year, which would reflect any increase in business during the year.

The amendment suggested in (B)(ii) of this paragraph establishes a new method for determining allowable reserve for the year 1963. Under this proposal, the determination of allowable reserve shall be made as of July 18, 1963 (the date on which securities which are initially designated must be owned). In the alternative, a company may compute the mean of its reserve at the beginning and the close of 1963. This figure, which can be readily ascertained, approximates the actual reserve figure on July 18, 1963. (The substance of present par. (4)(B) is now embodied in par. (3)(C).)

(g) *SALE OR LIQUIDATION OF WHOLLY OWNED FOREIGN SUBSIDIARY.* Page 28, line 23.

This is a new subsection (g). A revised subsection (g) appears below as subsection (i).

"(1) *IN GENERAL.—The tax imposed by section 4911 shall not apply to the acquisition by a United States person of a debt obligation of a foreign obligor if the debt obligation is acquired—*

"(A) *in connection with the sale by such United States person (or by one or more includible corporations in an affiliated group, as defined in section 48(c)(3)(C), of which such United States person is a*

member) of all of the outstanding stock, except for qualifying shares, of a foreign corporation; or

"(B) in connection with the liquidation by such United States person (or by one or more such includible corporations) of a foreign corporation all of the outstanding stock of which, except for qualifying shares, is owned by such United States person (or by one or more such includible corporations), but only if such debt obligation had been received by such foreign corporation as part or all of the purchase price in a sale of substantially all of its assets.

"(2) LIMITATION.—Paragraph (1) shall not apply to the acquisition of a debt obligation if any of the stock sold or surrendered in connection with its acquisition was originally acquired with the intent to sell or surrender.

This new provision is designed to exclude from application of the tax bona fide sales of wholly owned subsidiaries, where the transaction is motivated by factors other than the interest rate differential between American and foreign security markets. Debt obligations acquired by a U.S. person in connection with such a sale would be excluded from tax, regardless of whether the transaction involves a sale of stock or a sale of assets. The particular form of the sale is usually determined by the purchaser of the business involved, but the effect on the U.S. person will be the same in either situation. In the case of a sale of stock, the U.S. parent will acquire the debt obligations directly from the issuer. In the case of a sale of assets, the U.S. person will acquire the debt obligation upon the liquidation of its subsidiary, in exchange for the latter's stock. The proposal requires that the sale or surrender of stock involve all of the outstanding stock of a foreign corporation (except qualifying shares) and excludes the acquisition from tax unless the stock of the foreign corporation was originally acquired with the intent to sell or surrender.

(*h*) *CERTAIN DEBT OBLIGATIONS SECURED BY UNITED STATES MORTGAGES, ETC.* Following page 31, line 25.

This is a new subsection (h) of section 4914.

"(1) IN GENERAL.—The tax imposed by section 4911 shall not apply to the acquisition from a foreign obligor by a United States person of a debt obligation of such foreign obligor which is secured by real property located in the United States, to the extent—

"(A) the debt obligation is a part of the purchase price of such real property (or of such real property and related personal property), or

"(B) the debt obligation arises out of a loan made by such United States person to the foreign obligor the proceeds of which are concurrently used as part of the purchase price of such real property (or of such real property and related personal property).

"(2) LIMITATION.—Paragraph (1) shall apply to the acquisition of a debt obligation only if—

"(A) the owner of the property sold is a United States person, and

"(B) at least 25 percent of the purchase price of the property sold is, at the time of such sale, paid in United States currency to such United States person by the foreign obligor from funds not obtained from United States persons for the purpose of purchasing such property.

"(3) RELATED PERSONAL PROPERTY.—For purposes of paragraph (1), the term 'related personal property' means tangible personal property which is sold in connection with the sale of real property for use in the operation of such real property.

This provision is designed to prevent application of the tax in the case of a loan secured by real property located in the United States to finance the purchase of such real property by a foreigner involving a large cash downpayment (at least 25 percent of the sales price) to the U.S. seller. A transaction of this type has a favorable effect on our balance of payments, and would not have occurred if the financing were not available. Since the obligation is secured by U.S. real estate, there is no risk that the property involved will not remain in the United States, as would be the case with respect to personal property.

(i) *LOSS OF ENTITLEMENT TO EXCLUSION IN CASE OF CERTAIN SUBSEQUENT TRANSFERS.* Following new subsection (L) added following line 25 on page 31.

This is a revised subsection (g).

"(1) IN GENERAL.—

"(A) Where an exclusion provided by paragraph (1)(B), (2), (3), [or] (4), *or (5)* of subsection (c), or the exclusion provided by subsection (d), has applied with respect to the acquisition of a debt obligation by any person, but such debt obligation is subsequently transferred by such person (before the termination date specified in section 4911(d)) to a United States person otherwise than—

"(i) to any agency or wholly-owned instrumentality of the United States;

"(ii) to a commercial bank acquiring the obligation in the ordinary course of its commercial banking business; [or]

"(iii) in the case of an exclusion provided by paragraph (1)(B), (2), or (3) of subsection (c), to any transferee where the extension of credit by such person and the acquisition of the debt obligation related thereto were reasonably necessary to accomplish the sale of property or services out of which the debt obligation arose, and the terms of the debt obligation are not unreasonable in light of credit practices in the business in which such person is engaged; or

"[(iii)] *(iv)* in a transaction described in subsection (a)(1) or (2), or a transaction (other than a transfer by gift) described in subsection (a)(3),

then liability for the tax imposed by section 4911 (in an amount determined under subparagraph (D) of this paragraph) shall be incurred by the transferor (with respect to such debt obligation) at the time of such subsequent transfer.

"(B) Where the exclusion provided by paragraphs (2) *and* (3) of subsection (c) has applied with respect to the acquisition of stock by any person, but such stock is subsequently transferred by such person (before the termination date specified in section 4911(d)) to a United States person otherwise than in a transaction described in subsection (a)(1) or (2), or a transaction (other than a transfer by gift) described in subsection (a)(3), then liability for the tax imposed by section 4911 (in an amount determined under subparagraph (D) of this paragraph) shall be incurred by the transferor (with respect to such stock) at the time of such subsequent transfer.

The proposed change in subparagraph (A) liberalizes the provisions applicable to the transferability of debt obligations received by an exporter so as not to interfere with the legitimate export financing of U.S. companies. The bill now provides that export paper may be transferred only to an agency or wholly-owned instrumentality of the United States, a commercial bank in the ordinary course of its commercial banking business, or by operation of law. This proposal permits transfer to other U.S. persons, provided the original extension of credit by the exporter was reasonably necessary to accomplish the export, and the terms of the debt obligation are not unreasonable in light of credit practices in the exporter's business.

The proposed change in subparagraph (B) applies the restrictions applicable to the transfer of stock received in connection with the export financing of tangible personal property to intangible personal property, in accordance with new section 4914(c)(3).

Section 4915. EXCLUSION FOR DIRECT INVESTMENTS

(a) IN GENERAL. Page 32, line 2.

(1) EXCLUDED ACQUISITIONS. Page 32, line 3.

This paragraph should be amended to read as follows:

"Except as provided in subsections (c) and (d) of this section, the tax imposed by section 4911 shall not apply to the acquisition by a United States person (A) of stock or a debt obligation of a foreign corporation *or of a debt obligation from a foreign corporation which received such obligation in the ordinary course of its trade or business as a result of the sale or rental of products manufactured or assembled by it or of the performance of services by it*, if immediately after the acquisition such person (or one or more includible corporations in an affiliated group, as defined in section 1504, of which such person is a member) owns (directly or indirectly) 10 percent or more of the total combined voting power of all classes of stock of such foreign corporation, or (B) of stock or a debt obligation of a foreign partnership if immediately after the acqui-

sition such person owns (directly or indirectly) 10 percent or more of the profits interest in such foreign partnership. * * *

This proposed change extends the direct investment exclusion to the acquisition by a U.S. corporation of installment receivables acquired by its subsidiary in connection with the sale or rental of products manufactured or assembled by the subsidiary or the performance of services by the subsidiary.

Under the bill as presently drafted a U.S. corporation can lend funds to a foreign subsidiary and acquire a debt obligation in return tax free. In certain instances, the U.S. corporation may be restricted by trust indentures or other agreements in its ability to lend to a subsidiary. If this is the case, the U.S. corporation may be permitted under the trust indenture to finance its subsidiaries by acquiring the installment receivables received by the subsidiaries in the ordinary course of conducting their business. The proposed amendment recognizes this practice as an alternative to a direct investment and excludes acquisition of the receivables from the tax.

(2) OVERPAYMENT WITH RESPECT TO CERTAIN TAXABLE ACQUISITIONS. Page 32, line 23.

This paragraph should be amended to read as follows:

"The tax paid under section 4911 on the acquisition *by a United States person* of stock *or a debt obligation* of a foreign corporation or foreign partnership, *or a debt obligation from a foreign corporation which received such obligation in the ordinary course of its trade or business as a result of the sale or rental of products manufactured or assembled by it or of the performance of services by it*, [by a United States person] shall (unless this subsection is inapplicable by reason of subsection (c) or (d)) constitute an overpayment of tax if such person — [continuously holds such stock from the time of its acquisition to the last day of the calendar year in which the acquisition was made and as of such last day meets the ownership requirement of paragraph (1).]

"*(A) meets the ownership requirement of paragraph (1) with respect to such corporation or partnership at any time within 12 months after the date of such acquisition, and*

"*(B) holds the stock or debt obligation continuously from the date of such acqusition to the last day of the calendar year in which such ownership requirement is first met.*

Under regulations prescribed by the Secretary or his delegate, credit or refund (without interest) shall be allowed or made with respect to such overpayment.

This provision and proposed change are designed to avoid hardship in a case where a U.S. person is unable to satisfy in a single acquisition the 10 percent or more voting stock requirement of the direct investment provisions, but where he acquires the requisite 10-percent interest over a 12-month period. It also extends the credit or refund provisions to the acquisition of debt obligations under these circumstances.

The bill now provides an exclusion for acquisitions if a U.S. person

acquires stock in a foreign corporation or partnership in a series of transactions, if at the end of the calendar year involved the person holds a 10-percent or greater stock interest. The proposed change makes clear that the exclusion is available if the 10-percent interest is acquired in any 12-month period, whether or not the 12-month period coincides with a particular calendar year, and allows the credit or refund in the case of debt obligations acquired in such situations.

Section 4916. EXCLUSION FOR INVESTMENTS IN LESS DEVELOPED COUTRIES

(a) GENERAL RULE. Page 37, line 14.
Subsection (a) should be amended as follows:

"The tax imposed by section 4911 shall not apply to the acquisition by a United States person of—

"(1) a debt obligation issued or guaranteed by the government of a less developed country or a political subdivision thereof, or by an agency or instrumentality of such a government;

"(2) stock or a debt obligation of a less developed country corporation; **[or]**

"(3) a debt obligation issued by an individual or partnership resident in a less developed country in return for property which is used, consumed, or disposed of wholly within one or more less developed countries**[.]**; *or*

"(4) stock or a debt obligation of a foreign issuer or foreign obligor, to the extent that such acquisition is required as a reinvestment within a less developed country by the terms of a contract of sale to, or of a contract of indemnification with respect to the nationalization, expropriation, or seizure by, the government of such less developed country or a political subdivision thereof, or an agency or instrumentality of such government, of property owned within such less developed country or such political subdivision by such United States person, or by a controlled foreign corporation (as defined in section 957) more than 50 percent of the total combined voting power of all classes of stock entitled to vote of which is owned (within the meaning of section 958) by such United States person, but only if such contract was entered into because the government of such less developed country or political subdivision, or such agency or instrumentality—

"(A) has nationalized or has expropriated or seized, or has threatened to nationalize or to expropriate or seize, a substantial portion of the property owned within such less developed country or such political subdivision by such United States person or such controlled foreign corporation; or

"(B) has taken action which has the effect of nationalizing or of expropriating or seizing, or of threatening to nationalize or to expropriate or seize, a substantial portion of the property so owned.

New paragraph (4) is designed to exclude from the proposed tax the acquisition of securities of a company operating in a less developed country with the proceeds from the payment by the government of

that country or its instrumentality for the stock or assets of a business previously operated in that country by the U.S. person. The U.S. person must prove the payment for his property is an indemnification for the seizure of property or compelled under threat of expropriation. The U.S. person seeking an exclusion under this provision must also show that the reinvestment of the sales proceeds within the less developed country was required by the contract terms.

In the circumstances contemplated by the proposed amendment, the companies in which the U.S. person must reinvest presumably would qualify as less developed country corporations under the requirements of section 4916(c)(1), particularly in light of the interests of the less developed country. However, the officers of these companies are aware of the pressures on the U.S. person seeking reinvestment in these circumstances, and they are under no compulsion to reveal information regarding their assets and income which is required to establish less developed country corporation status. Such information is not otherwise available. Moreover, the contract generally requires reinvestment within a specified period of time, which increases the pressure on the U.S. person.

(c) LESS DEVELOPED COUNTRY CORPORATION DEFINED. Page 40, line 3.

(1) IN GENERAL. Page 40, line 5.

Paragraph (1) should be amended to read as follows and a new paragraph (2) should be added. Present paragraph (2) should be renumbered (3).

"For purposes of this section, the term 'less developed country corporation' means a foreign corporation which for the applicable periods set forth in paragraph [(2)] *(3)*—

"(A) meets the requirements of section 955(c) (1) or (2); or

"(B) [has gross income 80 percent or more of which is derived] *derives 80 percent or more of its gross income, if any,* from sources within less developed countries, *or from deposits in the United States with persons carrying on the banking business, or both,* and has assets 80 percent or more in value of which consists of—

"(*i*) property described in clauses (*ii*), (iii), (iv), and (v) of section 955(c)(1)(B),

"*(ii) property described in section 956(b)(1) (regardless of when acquired),*

"*(iii) debt obligations described in paragraph (3) of subsection (a) of this section, and*

"*(iv) obligations of the United States;*

except that in applying this paragraph the determination of whether a foreign country is a less developed country shall be made in accordance with subsection (b) of this section.

"*(2) SPECIAL RULES.—For purposes of subparagraphs (A) and (B) of paragraph (1)—*

"*(A) income derived from property described in section 956(b)(1) (regardless of when acquired) shall not be taken into account, and*

"(B) obligations of any other less developed country corporation shall be taken into account under section 955(c)(1)(B)(iii) without regard to the period remaining to maturity at the time of their acquisition.

For purposes of subparagraph (B) of paragraph (1) deposits outside the United States (other than deposits in a less developed country) with persons carrying on the banking business, and income from such deposits, shall not be taken into account.

The proposed changes in this subsection are designed to prevent disqualification of less developed country corporations from the exclusion from tax intended under this section because of investments in U.S. property or income derived from U.S. sources, or because of the fact that some of the corporation's assets consist of debt obligations of less developed country corporations which have a short-term maturity, or debt obligations of individuals or partnerships resident in less developed countries.

The criteria established in the present bill for determining less developed country corporation status were derived primarily from income tax concepts established in the Revenue Act of 1962. These criteria have been expanded in the manner described to accommodate them to the purposes of the interest equalization tax.

Section 4917. EXCLUSION FOR ORIGINAL OR NEW ISSUES WHERE REQUIRED FOR INTERNATIONAL MONETARY STABILITY

(b) APPLICABILITY OF EXECUTIVE ORDER. Page 35, line 13. This subsection should be amended to read as follows:

"An Executive order described in subsection (a) may be applicable to all such original or new issues or to any aggregate amount or classification thereof which shall be stated in such order and shall apply to acquisitions occurring during such period of time as shall be stated therein. If the order is applicable to a limited aggregate amount of such issues it shall apply (under regulations prescribed by the Secretary or his delegate) to those acquisitions as to which notice of acquisition was first filed, provided that in the case of any such notice the acquisition described in the notice is made before or within 90 days after the date of filing *or such longer period after such date as may be specified in such order.*

This change is necessary so that in the event the President deems it advisable to impose a limitation on the exclusion for original or new issues originating in a particular country the procedural requirements for administering such a limitation would be sufficiently flexible. If a limitation is imposed, it may be deemed appropriate to permit a longer period of time between the date of filing notice and the date of acquisition as to certain types of acquisitions where a 90-day limit is not feasible.

(c) ORIGINAL OR NEW ISSUE. Page 45, line 25. This subsection should be amended to read as follows:

"For purposes of this section—

"(*1*) stock shall be treated as part of an original or new issue only when it is acquired from the issuer by the United States person claiming the exclusion; and

"(2) a debt obligation shall be treated as part of an original or new issue only if acquired not later than [60] *90* days after the date on which interest begins to accrue on such obligation, *except that a debt obligation secured by a lien on improvements on real property which are under construction or are to be constructed at the time such obligation is issued (or if such obligation is one of a series, at the time the first obligation in such series is issued) shall be treated as part of an original or new issue if—*

"(A) such obligation is acquired not later than 90 days after the date on which interest begins to accrue on the total amount of such obligation (or if such obligation is one of a series, on the last issued of the obligations in such series); and

"(B) the United States person claiming the exclusion became committed to the acquisition of such obligation not later than 90 days after the date on which interest began to accrue on any part of such obligation (or, if such obligation is one of a series, on the first obligation issued in such series).

The proposed change as to the definition of a new issue where a construction loan is involved is necessary so that such loans are eligible to qualify under this exclusion. Typically, the U.S. person may not acquire the debt obligation involved until construction has been completed and several months have elapsed since interest began to accrue on the obligation. Accordingly, the proposed change would commence the 90-day period after interest began to accrue on the total obligation (or if a series of obligations is involved, the last-issued obligation in the series), provided the U.S. person was committed to acquire the obligation within 90 days after interest began to accrue on any part of the obligation (or if a series of obligations is involved, the first issued).

Section 4918. EXEMPTION FOR PRIOR AMERICAN OWNERSHIP

(a) GENERAL RULE. Page 46, line 9.

This subsection should be amended as follows:

"The tax imposed by section 4911 shall not apply to an acquisition of stock or a debt obligation of a foreign issuer or obligor if it is established *in the manner provided in this section* [by clear and convincing evidence] that the person from whom such stock or debt obligation was acquired was a United States person throughout the period of his ownership or continuously since July 18, 1963 *and was a United States person eligible to execute a certificate of American ownership with respect to such acquisition.*

This change, together with the amendment proposed in subsection (f) below, is intended to make clear that in cases where a confirmation received from a member of a national securities exchange or the National Association of Securities Dealers does not serve as proof of prior American ownership, a purchaser claiming an exemption based on prior American ownership must produce a certificate of American ownership to substantiate his claim, unless the failure to produce a certificate is due to reasonable cause. In the overwhelming majority

of acquisitions through American broker-dealers, a confirmation will serve as proof of prior American ownership. In those cases where a confirmation is not received, a certificate of American ownership must be obtained in order to establish the exemption. It is proposed that this certificate requirement be made mandatory in order to forestall possible evasion of the tax by Americans who purchase from other Americans who are being treated as foreigners for a particular purpose under the bill. For example, a U.S. person purchasing from a dealer who claims a credit or refund under section 4919 should not be permitted to assert the exemption for prior American ownership since the dealer can not execute the requisite certificate in connection with the transaction.

(c) TRADING ON CERTAIN NATIONAL SECURITIES EXCHANGES. Page 46, line 23.

This subsection should be amended to read as follows:

> "For purposes of subsection (a), a written confirmation, received from a member or member organization of a national securities exchange registered with the Securities and Exchange Commission [stating that an acquisition was made in the regular market on such exchange (and not subject to a special contract)] *in connection with an acquisition on such exchange, which does not state that such acquisition was made subject to a special contract* shall be conclusive proof for purposes of this exemption of prior American ownership * * *

The proposed change conforms the language of the bill to the rules adopted by national securities exchanges in connection with the trading of foreign securities subject to the tax. Under exchange rules, a purchaser in the regular market on the exchange is assured that he is acquiring from another American and, accordingly, is not liable for the tax or required to file a return. The purchaser's confirmation, which does not contain a statement that his acquisition is subject to the tax, is considered conclusive proof of prior American ownership.

(f) *OTHER PROOF OF EXEMPTION.* Following page 50, line 5.

This is a new subsection.

> *"For purposes of subsection (a), if a person establishes, with respect to an acquisition, that there is reasonable cause for his inability to establish prior American ownership under subsection (b), (c) or (d), he may establish prior American ownership for purposes of this exemption by other evidence that the person from whom such acquisition was made was a United States person eligible to execute a certificate of American ownership with respect to such acquisition.*

This suggested amendment is proposed for the reasons set forth above under subsection (a).

Section 4919. SALES BY UNDERWRITERS AND DEALERS TO FOREIGN PERSONS

(a) CREDIT OR REFUND. Page 50, line 8.

(1) PRIVATE PLACEMENTS and (2) PUBLIC OFFERINGS. Page 50, line 12, and page 50, line 19.

These two paragraphs should be deleted and a new consolidated paragraph should be substituted to read as follows:

"(*1*) *PRIVATE PLACEMENTS AND PUBLIC OFFERINGS.—Are acquired by an underwriter in connection with a private placement or a public offering by a foreign issuer or obligor (or a person or persons, directly or indirectly, controlling, controlled by, or under common control with such issuer or obligor) and are sold as part of such private placement or public offering by the underwriter (including sales by other underwriters who are United States persons participating in the placement or distribution of the stock or debt obligations acquired by the underwriter) to persons other than United States persons;*

This proposed revision will equalize the treatment of foreign underwritings, whether in the form of a public offering or private placement, and prevent the loss of the credit or refund for resales to foreigners because of distribution practices prevailing in a particular foreign country.

The bill presently requires that the underwriter in a private placement sell directly to foreigners to qualify for the credit or refund while in the case of public offerings, the sales to foreigners may be made by selling group members. In some foreign countries, the concept of "private placement" includes offerings where selling groups are utilized. The proposed change will eliminate the distinction between the treatment of private placements and public offerings and will allow the credit or refund in all underwriting situations where the foreign stock or debt obligations are placed with foreign investors, and U.S. persons are only part of the distribution and placement process.

(*2*) *Certain debt obligations.* Page 51, line 4.

This paragraph which was formerly (3) should be amended to read as follows:

"Consist of debt obligations—

"(*A*) acquired by a dealer in the ordinary course of his business and sold by [the dealer to persons other than United States persons within 90 days after (or, in the case of short sales, within 90 days before) their acquisition] *him, within 90 days after their purchase, to—*

"(i) persons other than United States persons, or

"(ii) another dealer who resells them on the same or the next business day to persons other than United States persons; or

"(B) acquired by a dealer in the ordinary course of his business to cover short sales made by him, within 90 days before their purchase, to—

"(i) persons other than United States persons, or

"(ii) another dealer who resold them on the same or the next business day to persons other than United States persons.

This proposed change will insure that the credit or refund available to dealers in case of the sale of foreign bonds to foreigners within 90 days after acquisition is not lost because of the form of the transaction. This provision now requires that in order to qualify for the credit or refund the dealer must sell to a foreign person within 90 days after acquisition. However, a substantial percentage of the transactions of this type involve a sale by the U.S. dealer to another U.S. dealer who in turn sells to a foreigner. The second U.S. dealer normally does not buy unless he has a foreign customer prepared to purchase from him. The proposed change recognizes this practice and permits the credit or refund, provided the second dealer sells to a foreigner on the same day as he purchases from the first dealer or the next business day.

(3) *Certain stock.* Page 51, line 4.

This is a new paragraph (3).

> "*Consist of stock acquired by a dealer in the ordinary course of his business and sold by him, on the same business day on which they were purchased, to persons other than United States persons.*
>
> Under regulations prescribed by the Secretary or his delegate, credit or refund (without interest) shall be allowed or made with respect to such overpayment. *For purposes of paragraphs (2) and (3) of this subsection and for purposes of paragraph (3) of subsection (b), the day of purchase or sale of any stock or debt obligation is the day on which an order to purchase or to sell, as the case may be, is executed.*

This new paragraph is designed to permit dealers in securities to be able to conduct certain types of arbitrage transactions in stocks without at the same time weakening the effectiveness of the tax. The last sentence of the provision makes clear that the purchase or sale date is the day on which the buy or sell order is executed, for purposes of this provision and the bond provision of (2) above.

The present bill does not contain a provision allowing a credit or refund where dealers acquire foreign stocks and sell to foreigners. This has had the effect of limiting certain types of arbitrage activities on exchanges. To alleviate this problem, the proposed change allows a credit or refund where a dealer sells foreign stock to a foreign person on the same day the stock is purchased. This proposal does not contain a 90-day provision as in the case of bonds because of the possibility that a broad dealer exclusion in stocks could become a tax-free vehicle for speculation in foreign securities.

(b) EVIDENCE TO SUPPORT CREDIT OR REFUND. Page 51, line 13.

The contents of present subsection (b) are incorporated in paragraphs (1) and (2) of new subsection (b). Paragraph (3) is entirely new.

> "*(1) IN GENERAL.—Credit or refund shall be allowed to an underwriter or dealer under subsection (a) with respect to any stock or debt obligation sold by him only if the underwriter or dealer—*
>
> "*(A) files with the return required by section 6011 (d) on which credit is claimed, or with the claim for*

refund, such information as the Secretary or his delegate may prescribe by regulations, and

"(B) establishes that such stock or debt obligation was sold to a person other than a United States person.

In any case where two or more underwriters form a group for the purpose of purchasing and distributing (through resale) stock or debt obligations of a single foreign issuer or obligor, any one of such underwriters may, to the extent provided by regulations prescribed by the Secretary or his delegate, satisfy the requirements of this paragraph on behalf of all such underwriters.

"(2) CERTAIN SALES BY UNDERWRITERS.—For purposes of paragraph (1)(B), in the case of a claim for credit or refund under subsection (a)(1) with respect to stock or a debt obligation acquired by an underwriter and not sold by him directly to a person other than a United States person, a certificate of sale to a foreign person (setting forth such information, and filed in such manner, as the Secretary or his delegate may prescribe by regulations), executed by the underwriter who made such sale, shall be conclusive proof that such stock or debt obligation was sold to a person other than a United States person, unless the underwriter relying upon the certificate has actual knowledge that the certificate is false in any material respect.

"(3) SALES BY DEALERS.—

"(A) SALES ON NATIONAL SECURITIES EXCHANGES.—For purposes of paragraph (1)(B), in the case of a claim for credit or refund under subsection (a)(2), the sale by a dealer of a debt obligation on a national securities exchange registered with the Securities and Exchange Commission subject to a special contract (and not in the regular market) shall be conclusive proof that such debt obligation was sold to a person other than a United States person, if such exchange has in effect at the time of the sale rules providing that—

"(i) a member or member organization of such exchange selling a debt obligation as a dealer, or effecting the sale as broker of a debt obligation on behalf of a dealer, on such exchange subject to a special contract (and not in the regular market) shall furnish to the member or member organization purchasing such debt obligation as a dealer, or effecting the purchase as broker of such debt obligation on behalf of a dealer, a written confirmation or comparison stating that such sale is being made as a dealer, or on behalf of a dealer; and

"(ii) if the purchaser of such debt obligation is a dealer (whether or not a member or member organization of such exchange), the terms of the contract applicable to such sale shall require the purchasing dealer to undertake to resell such debt

obligation on the day of purchase or the next business day to a person other than a United States person.

A dealer who acquires a debt obligation in a transaction in which a written confirmation or comparison described in clause (i) is furnished shall not be entitled to a credit or refund under subsection (a)(2) with respect to his acquisition of such debt obligation unless he establishes that such debt obligation was sold by him on the day on which it was purchased or the next business day to a person other than a United States person.

"(B) Over-the-counter sales.—For purposes of paragraph (1)(B), in the case of a claim for credit or refund under subsection (a)(2) with respect to a debt obligation sold in a transaction not on a national securities exchange, a written confirmation furnished by a member or member organization of a national securities association registered with the Securities and Exchange Commission stating that such member or member organization—

"(i) effected the purchase as broker of a debt obligation on behalf of a person other than a United States person, or

"(ii) purchased a debt obligation which he resold on the day of purchase or the next business day to a person other than a United States person,

shall be conclusive proof that such debt obligation was sold to a person other than a United States person (unless the dealer relying upon the confirmation has actual knowledge that the confirmation is false in any material respect), if such association has in effect at the time of the purchase rules providing that a member or member organization who effects a purchase of, or purchases, a debt obligation from a dealer who notifies such member or member organization that such debt obligation is being sold by such dealer and that such dealer intends to claim a credit or refund under subsection (a) (2), shall furnish to such dealer a written confirmation stating that the purchase of such debt obligation was (or was not) effected by such member or member organization on behalf of a person other than a United States person, or that such debt obligation was (or was not) sold by such member or member organization on the day of purchase or the next business day to a person other than a United States person.

Paragraphs (1) and (2) of this subsection make clear that if two or more underwriters form a group for the purpose of distributing securities of a foreign issuer or obligor, any one member of the group may claim the credit or refund provided in this section for sales to foreign persons on behalf of the other members of the group. If the underwriter filing the claim on behalf of the group has not himself sold directly to foreigners, he may rely on certificates of sale to foreign

persons executed by the other underwriters, unless the filing underwriter has actual knowledge the certificates are false in any material respect. The essence of these two paragraphs now appear in subsection (b) in the present bill.

Paragraph (3) of this subsection is designed to provide a means under which a dealer claiming a credit or refund under section 4919 (a)(2) for the sale of foreign bonds to foreigners within 90 days after their purchase can establish the bonds were actually sold to foreigners.

The proposed provision establishes separate procedures to prove sale to a foreigner with respect to the over-the-counter and exchange markets because of the different characteristics of these markets. In the case of national securities exchanges, a dealer can establish sale to a foreigner if he sells in the special "F" market for foreign securities maintained by the exchange, provided the exchange has adopted the required rules. These rules must provide that a dealer acquiring bonds on the exchange in the special "F" market from another dealer who is claiming a credit or refund under section 4919(a)(2) must receive a special confirmation or comparison to this effect, and must undertake to resell the bonds to a foreigner on the date of purchase or the next business day. In the over-the-counter market, where transactions are on a negotiated basis, a dealer can establish sale to a foreigner by a confirmation received from a member of the National Association of Securities Dealers stating that the bonds were acquired by the member on behalf of a foreigner, or were sold by the member to a foreigner on the date of purchase or the next business day, provided the selling dealer has no actual knowledge the confirmation is false in any material respect and the association has adopted the requisite rules.

Section 4920. *DEFINITIONS; SPECIAL RULES*

(b) *Special Rule for Foreign Underwriters.* Following page 60, line 2.

The following is a new subsection (b). Present subsection (b) should become (c).

> "*(b) Special Rule for Foreign Underwriters.—A partnership or corporation which is not a United States person and which participates, as an underwriter in an underwriting group that includes one or more United States persons, in a public offering of stock or debt obligations of a foreign issuer or obligor shall, if such partnership or corporation so elects and subject to such terms and conditions as the Secretary or his delegate may prescribe by regulations, be treated as a United States person for purposes of this chapter with respect to its participation in such public offering.*

This new subsection is designed to afford uniform treatment to American purchasers of foreign securities in underwritings in which a foreign underwriter is participating together with U.S. underwriters.

Under the present provisions of the bill, the managing underwriter would be required to allocate to each U.S. purchaser the pro rata share of his purchase attributable to the foreign underwriter's participation. No certificate of American ownership could be given to

the customer with respect to this portion of his purchase, and interest equalization tax would be due. As a result, the underwriters would have to make the taxable portion available to Americans at a discounted price, in order to absorb the cost of the tax for the purchaser. The proposed amendment will permit the foreign underwriter to assume the tax burden directly, by electing to be treated as a U.S. person with respect to his participation, and thereby allow uniform pricing of the issue to U.S. purchasers. The proposal also will eliminate the necessity for individual U.S. purchasers to file returns and will simplify administration of the tax.

Section 2(c). *Effective Date.*

(2) *Preexisting commitments.* Page 60, line 13.

This paragraph should be amended as follows:

> Such amendments shall not apply to an acquisition—
>
> (A) made pursuant to an obligation to acquire which on July 18, 1963—
>
> (i) was unconditional, or
>
> (ii) was subject only to conditions contained in a formal contract under which partial performance had occurred;
>
> (B) as to which on or before July 18, 1963, the acquiring United States person (or, in a case where 2 or more United States persons are making acquisitions as part of a single transaction, a majority in interest of such persons) had taken every action to signify approval of the acquisition under the procedures ordinarily employed by such person (or persons) in similar transactions and had sent or deposited for delivery to the foreign [issuer or obligor] *person from whom the acquisition was made* written evidence of such approval in the form of a commitment letter, memorandum of terms, *draft purchase contract*, or other [signed] document setting forth *or referring to a document sent by the foreign person from whom the acquisition was made which set forth* the principal terms of such acquisition, subject only to the execution of formal documents evidencing the acquisition and to customary closing conditions;
>
> *(C) if, on or before July 18, 1963, the acquiring United States person—*
>
> *(i) had entered into a contract for the sale to the government of a less developed country or a political subdivision thereof, or an agency or instrumentality of such government, of property owned within such less developed country or political subdivision by such person or by a controlled foreign corporation (as defined in section 957) more than 50 percent of the total combined voting power of all classes of stock entitled to vote of which is owned (within the meaning of section 958) by such person, or of stock or debt obligations of such a controlled foreign corpora-*

tion which was actively engaged in the conduct of a trade or business within such less developed country; or had entered into a contract of indemnification with respect to the nationalization, expropriation, or seizure of such property or of such stock or debt obligations by the government of a less developed country or political subdivision thereof, or an agency or instrumentality of such government, or

(ii) had sent or deposited for delivery to the government of a less developed country or political subdivision thereof, or agency or instrumentality of such government, a commitment letter, memorandum of terms, or other document setting forth the principal terms of a contract described in clause (i),

to the extent such acquisition is req[illegible]red by the terms of the contract as a reinvestment within such less developed country of amounts equal to part or all of the consideration received under the contract; or

[C] *(D)* which would be excluded from tax under section 4915 of the Internal Revenue Code of 1954 but for the provisions of subsection (c) thereof, if (i) on or before July 18, 1963, the acquiring United States person applied for and received from a foreign government (or an agency or instrumentality thereof) authorization to make such acquisition and approval of the amount thereof, and (ii) such authorization was required in order for such acquisition to be made.

The purpose of this provision and the suggested changes are to exclude from tax acquisitions resulting from transactions which were completed or in advanced stages of negotiation on July 18, 1963. Application of tax to these acquisitions might create substantial hardship.

The proposed changes in subparagraph (B) make clear that a draft purchase agreement, which normally would not be signed by the lender, constitutes sufficient evidence of approval by the lender of the acquisition, provided that the draft purchase agreement was furnished to the borrower on or before July 18, 1963, and the lender had approved the acquisition in accordance with its customary procedures on or before that date. The changes also clarify that the acquisition need not be made directly from the foreign issuer or obligor, but can be made from another foreign person, so long as the other requirements of the provision are satisfied.

Proposed subparagraph (C) excludes from application of the tax the acquisition of stock or debt obligations pursuant to a contract or commitment entered into prior to July 18, 1963, under which a U.S. person sells property located in a less developed country (or stock of a company engaged in business in such a country) to, or receives indemnification from, such a less developed country (or its agency, instrumentality, or subdivision). This new provision is comparable to new section 4916(a)(4). Under both provisions, the companies in

which the U.S. person must reinvest would presumably qualify as less developed country corporations under the requirements of section 4916(c)(1). However, these companies are aware of the pressures on the U.S. person to reinvest the proceeds of sale, and they are not compelled to reveal the information regarding their assets and income which is necessary to establish compliance with the less developed country corporation provisions. This information is not otherwise available.

(7) DOMESTICATION. Page 63, line 22.

This paragraph should be amended to read as follows:

> Such amendments shall not apply to the acquisition by a domestic corporation of the assets of a foreign corporation pursuant to a reorganization described in subparagraph (C), (D) or (F) of section 368(a)(1) of the Internal Revenue Code of 1954 if the acquisition occurs on or before the 180th day after the date of the enactment of this Act and the foreign corporation was a management company registered under the Investment Company Act of 1940 from July 18, 1963, until the time of the acquisition.

This proposed amendment makes clear that a foreign investment company which domesticates within 180 days after enactment of this bill may do so in a reorganization under subparagraph (C) of section 368(a)(1) of the Internal Revenue Code as well as subparagraph (D) or (F) of that section.

Section 3 RETURNS

(a) MAKING OF RETURNS. Page 64, line 12.

(1) IN GENERAL. Page 64, line 19.

This paragraph should be amended to read as follows:

> "Every person shall make a return for each calendar quarter during which he incurs liability for the tax imposed by section 4911, or would so incur liability but for the provisions of section 4918. The return shall, in addition to such other information as the Secretary or his delegate may by regulations require, include a list of all acquisitions made by such person during the calendar quarter which are exempt under the provisions of section 4918, and shall, *with respect to each such acquisition, be accompanied either (A) by a certificate of American ownership which complies with the provisions of section 4918(e), or (B) in the case of an acquisition for which other proof of exemption is permitted under section 4918(f), by a statement setting forth a summary of the evidence establishing such exemption and the reasons for the person's inability to establish prior American ownership under subsection (b), (c), or (d) of section 4918* [be accompanied by clear and convincing evidence showing that the acquisitions are so exempt]. No return or accompanying evidence shall be required under this paragraph in connection with any acquisition with respect to which a written confirmation, furnished in

> accordance with the requirements described in section 4918 (c) or (d), is treated as conclusive proof of prior American ownership; nor shall any such acquisition be required to be listed in any return made under this paragraph.

This proposed amendment, like the suggested changes in section 4918 (a) and (b), is intended to facilitate the administration and enforcement of the interest equalization tax by requiring the filing of a certificate of American ownership with the quarterly tax return in order to prove the exemption for prior American ownership, unless the taxpayer can establish that his inability to file such a certificate is due to reasonable cause. No return or submission of proof is required if the acquisition was made through a member of a national securities exchange or the National Association of Securities Dealers who furnishes a confirmation to the purchaser which does not state that the purchase was subject to the tax. If a U.S. person is claiming the prior American ownership exemption but does not have the requisite certificate or confirmation, this proposed amendment requires him to attach a statement to his quarterly return setting forth a summary of the evidence establishing the exemption and the reasons for his inability to establish the exemption by means of a certificate or confirmation.

(3) REPORTING REQUIREMENTS FOR MEMBERS OF EXCHANGES AND ASSOCIATIONS. Page 65, line 20.

This paragraph should be amended to read as follows:

> "*Every* member[s] *or* [of] member organization[s] of *a* national securities exchange[s] *or of a* [and] national securities association[s] registered with the Securities and Exchange Commission shall keep such records and file such information as the Secretary or his delegate may by regulations prescribe in connection with *acquisitions and* sales effected by such member[s] or member organization[s] as *a* broker[s], and acquisitions made for [their own accounts,] *the account of such member or member organization*, of stock or debt obligations—
>
> "(A) as to which a certificate of American ownership or blanket certificate of American ownership is executed and filed *with such member or member organization as prescribed under* [as described in] section 4918(e)*; and*
>
> *"(B) as to which a written confirmation is furnished to a United States person stating that the acquisition—*
>
> *"(i) in the case of a transaction on a national securities exchange, was made subject to a special contract, or*
>
> *"(ii) in the case of a transaction not on a national securities exchange, was from a person who had not filed a certificate of American ownership with respect to such stock or debt obligation or a blanket certificate of American*

ownership with respect to the account from which such stock or debt obligation was sold.

The suggested additions to the recordkeeping requirements for brokers are essential to provide necessary enforcement procedures for collection of the proposed tax.

Under the bill, a broker who sells on behalf of a customer in the regular market and who does not advise the purchasing broker that he is acting on behalf of a foreigner, permits the purchasing broker to supply a confirmation to the purchaser which is conclusive proof of an exemption from the tax. Such selling brokers are required to retain appropriate records in connection with these transactions. In addition, brokers acting on behalf of the purchaser and seller in taxable transactions should also be required to maintain necessary records. Without such information and records, administration of the tax would be seriously handicapped.

Section 5. *Original Issue Discount*

This is a new section which should begin on page 67, line 17. Present section 5 (Penalties) should be renumbered section 6 Section 5 should provide as follows:

> "*Section 1232(b)(2) (relating to definition of issue price) is amended by inserting before the period at the end of the second sentence thereof the following: 'increased by the amount, if any, of tax paid under section 4911 (and not credited, refunded, or reimbursed) on the acquisition of such bond or evidence of indebtedness by the first buyer.'*

This new section is designed to remove the possibility that the purchaser of a debt obligation in a private placement might suffer adverse income tax consequences because of the interest equalization tax.

The purposes of the proposed tax have no relation to the treatment under section 1232 of the Internal Revenue Code of the part of the gain on a sale or exchange of debt obligations consisting of "original issue discount," and allocable to the period the taxpayer held the securities, as ordinary income. In the case of a private placement of debt obligations of a foreign issuer, where the amount of tax payable by a United States purchaser is reflected in a deduction from the purchase price, the amount of the discount might produce original issue discount and subject the purchaser and subsequent purchasers to possible additional ordinary income taxes. The proposed new section would avoid that unintended result.

Section 6. Penalties

Section 6681. FALSE EQUALIZATION TAX CERTIFICATES. Page 68, line 13.

(d) *False Confirmations or Comparisons Furnished by Dealers.* Page 70, line 11.

This is a new subsection (d); present subsection (d) becomes (e).

> "*(1) MEMBERS OF NATIONAL SECURITIES EXCHANGES.—A member or member organization of a national securities exchange described in section 4919(b)(3)(A) who, in a transaction subject to the rules of such exchange as described in such section, wilfully furnishes a written confirmation or comparison which*

contains a misstatement of material fact or which fails to state a material fact shall be liable to a penalty equal to 125 percent of the amount of the tax imposed by section 4911 on the acquisition of the debt obligation by the dealer for whose benefit such confirmation or comparison is furnished.

"(2) *DEALERS.—Any person who sells as a dealer a debt obligation in a transaction subject to the rules of a national securities exchange as described in section 4919(b)(3)(A), in which such sale is effected on his behalf by a member or member organization of such exchange, and who wilfully fails to disclose to such member or member organization that such sale is being made by him as a dealer, shall be liable to a penalty equal to 125 percent of the amount of the tax imposed on his acquisition of the debt obligation with respect to which such confirmation or comparison is furnished.*

"(3) *MEMBERS OF NATIONAL SECURITIES ASSOCIATIONS.—A member or member organization of a national securities association described in section 4919(b)(3)(B) who wilfully furnishes a written confirmation described in such section (in a transaction subject to the rules of such association as described in such section) which contains a misstatement of material fact or which fails to state a material fact shall be liable to a penalty equal to 125 percent of the amount of the tax imposed by section 4911 on the acquisition of the debt obligation by the dealer for whose benefit such confirmation is furnished.*"

This new subsection provides penalties for members of national securities exchanges and the National Association of Securities Dealers who willfully violate the procedures set forth in section 4919(b)(3). That section permits a dealer claiming a credit or refund under section 4919(a)(2) (for the sale of foreign bonds to foreigners within 90 days after their purchase) to establish the bonds were actually sold to foreigners. The procedures in the over-the-counter market and on the exchanges require that the confirmations or comparisons furnished to the dealer on which the claim for credit or refund are based be truthful. This new subsection imposes a 125-percent penalty on a member or dealer who wilfully furnishes a false confirmation or comparison or who wilfully fails to disclose that he is acting as a dealer in a transaction described in section 4919(b)(3), since the false document or statement permitted a credit or refund to be obtained improperly.