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THE ALIEN AND THE FEDERAL TAX LAW

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I. WHO ARE ALIENS?

In a consideration of this subject, the first question which must be decided is: When is an alien considered a resident for tax purposes?

Generally, an alien, by reason of his status as such, is presumed to be a non-resident alien. This presumption may, however, be overcome. An alien who has filed his declaration of intention to become a citizen remains an alien until his final citizenship papers are granted.¹ A foreign born child residing in the United States who is a minor at or subsequent to the time of his father's naturalization becomes a citizen,² except that he cannot expatriate himself during his minority.³ Loss of citizenship is determined by the rules of the Nationality Act of 1940.⁴

Under present law, since March 3, 1931, a female citizen of the United States does not lose her status as such by reason of her marriage to an alien, in the absence of formal renunciation before a court having jurisdiction over naturalization of aliens. Conversely, an alien woman does not become a United States citizen by reason of her marriage to a citizen of the United States or by reason of her husband's naturalization. An alien woman may herself become naturalized, if she is otherwise eligible, even though her husband is ineligible for citizenship.⁵

A. RESIDENCE

The Federal Income Tax Law divides aliens into three classes: (1) Resident aliens, (2) non-resident aliens engaged in business within the United States and (3) non-resident aliens not engaged in business within the United States. The last class is subdivided into those having

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¹ Sec. 29, 11-3.

² OD 695, CB 3, 74 (1920).

³ OD 1085, CB 5, 191 (1921).

⁴ Sec. 29, 11-3.

⁵ IT 2601, CBX-2, 89 (1930).

a United States gross income of up to \$15,400.00 per year and those having a gross income in excess of this figure.⁶

There is no clear-cut definition of the term "residence" in the Income Tax Law; the question must be determined by the facts in each case.⁷ An individual's place of birth is his first residence. He can change it if he chooses to do so, and his intention is the fundamental test. Intention can be determined by declarations, conduct, character, temperament and similar manifestations.⁸ Other facts considered are whether the individual was joined by his family,⁹ statements made by the taxpayer in his will,¹⁰ and statements made by him to immigration authorities to obtain re-entry permits.¹¹

An alien actually present in the United States who is not a mere transient or sojourner is a resident within the meaning of the Income Tax Law, even though he has his legal domicile in another country.¹² He is not a transient if he lives in the United States with no definite intention as to his stay, even though he may have a vague, floating intention to return to another country at some indefinite time in the future.¹³

Where, however, an individual comes to the United States for a definite purpose which may be promptly accomplished, his intention to return immediately on fulfillment of his mission will ordinarily prevent his presence here from constituting residence.¹⁴ An alien singer who came to the United States and remained for short periods of time to fulfill his professional engagements did not acquire the status of a resident.¹⁵ Similarly, employees of a foreign railroad operated by a foreign government who were sent temporarily to an office maintained in the United States for the purpose of studying railroad conditions remained non-resident aliens.¹⁶ On the other hand, if the alien's mission requires him to make his home in this country for an extended time, his stay here will constitute residence despite any definite intention to return when his purpose is accomplished.¹⁷

An alien whose stay is limited to a short period by the immigration laws is considered as a non-resident alien in the absence of exceptional circumstances.¹⁸ Thus, an alien who fled to the United States from

⁶ Treasury Reg. 111, Secs. 29, 211-1, 29, 211-7, Mimeo. 5883, 1945 CB 244.

⁷ L. B. Peoples, 27 BTA 879.

⁸ Bank of N.Y. & Trust Co. (Valentine Estate), 21 BTA 197 (A).

⁹ J. P. Schumacher, 32 BTA 1242 (A).

¹⁰ Farmers Loan & Trust Co. v. U.S., 60 F.2d 618.

¹¹ L. E. L. Thomas, 33 BTA 725.

¹² Bowring v. Bowers, 24 F.2d 918, cert. den. 277 U.S. 608.

¹³ Sec. 29, 211-2.

¹⁴ *Ibid.*, n. 13.

¹⁵ Ingram Adm'x. (Caruso Estate) v. Bowers, 47 F.2d 925, aff'd., 57 F.2d 65.

¹⁶ I.T. 2018, CB III-1, 209 (1924).

¹⁷ *Supra*, n. 13.

¹⁸ *Supra*, n. 13.

wartime Europe under a temporary visitor's visa was considered a non-resident alien,¹⁹ as was an alien whose presence in the United States was based on several extensions of a deportation order.²⁰

However, an alien who resided in the United States for a year was presumed to be a residential alien, the presumption being rebuttable by evidence showing that he was a transient.²¹ A non-resident alien who served in the United States Army for a year was also considered a resident.²² The Fourth Circuit Court denied non-resident status to an alien who remained here during World War II through receipt of visa extensions granted because of wartime travel conditions.²³ A Philippine citizen who came here in connection with her daughter's education and decided to stay because of the danger of war was held to be a resident even though her entry and stay were limited to definite periods by the immigration laws.²⁴ Her husband, who stayed only so long as his business kept him in the United States, was held to be a non-resident.²⁵ Members of the family of a foreign ambassador or minister are considered as non-resident aliens for income tax purposes.²⁶

An alien who alleged New York residence in a divorce action was held to be a resident for tax purposes.²⁷

In the case of *Jesus Laguana v. Ansell*, in the District Court of Guam, on February 28, 1952, the Court held that the application of the Income Tax Law to Guam is to be on a territorial basis. Thus, the Guamanian authorities may require withholding and payment into the local treasury, and also that federal authorities do not administer the tax. In addition, it was held that a citizen of Guam who is a citizen of the United States only because of collective naturalization under the Organic Act of Guam is subject to U.S. tax only on income from United States sources. He is also subject to Guam tax imposed under the United States Income Tax Law.²⁸ It is the writers' opinion that a taxpayer who is liable for both U.S. and Guam taxes on income from a United States source can credit the United States tax against his Guam tax.

In another case, petitioner, a citizen of New Zealand and an official of the League of Nations, entered the United States temporarily in

¹⁹ Marie Anne DeGoldschmidt-Rothchild, 9 TC 325, aff'd., 168 F.2d 975.

²⁰ Florica Constantinescu, 11 TC 36 (A).

²¹ OD 197, CB I, 164 (1919).

²² OD 117, CB I, 163 (1919).

²³ Com. v. Zareh Nubar, 185 F.2d 584, rev'g 13 TC 566, pet. for rehearing den (CA-4), Dec. 20, 1950, cert. den. 71 S.Ct. 796.

²⁴ Mary A. Marsman, TC Memo Dkt. No. 18590, Feb. 21, 1950.

²⁵ J. H. Marsman, TC Memo Dkt. No. 18590, Feb. 21, 1950.

²⁶ OD 198, CB I, 164 (1919).

²⁷ Cristina de Bourbon Patino, 13 TC 816, aff'd 186 F.2d 962; 205 F.2d 338; 22 TC 91; 3 Am. Law. Rep. (2nd Series) 387.

²⁸ Rev. Rul. 56, IRB 1953-8, 6.

1940 in order to continue his official work, the pursuit of which was at Geneva, Switzerland. He was hampered by the war. He and his family lived at Princeton, N.J. in a rented apartment which he furnished, having given up his living quarters in Geneva on leaving there, and he conducted his official duties at Princeton until July, 1946. The Court held that "petitioner was a resident alien within the meaning of Section 29.11-2, Reg. 111."²⁹

The Internal Revenue Code defines the "United States" as including, for tax purposes only, the states, territories of Alaska and Hawaii, and the District of Columbia.³⁰ Therefore, residents of a "possession of the United States," such as Puerto Rico, the Virgin Islands or Guam are not, by reason of such residence, residents of the United States.³¹ Thus an alien bona fide resident of Puerto Rico during an entire taxable year, while he is taxed in the same manner as a resident of the U.S., is entitled to an exclusion from gross income in the amount of income derived from sources within Puerto Rico. Section 29.397-8, Reg. 111, provides that "the term 'non-resident alien' includes a non-resident individual and a non-resident alien fiduciary." The Internal Revenue Code does not define "resident" or "non-resident" in this area, thus leaving it to administrative and judicial determinations. The Internal Revenue Bureau has construed residence to mean something less than domicile.³²

B. ALIEN SEAMEN AS RESIDENT ALIENS

An alien seaman may establish residence in the United States by making his home on a vessel engaged in coast-side trade. The mere fact that he makes his home on a vessel engaged in foreign trade will not constitute residence in the United States even though the vessel flies the American flag and touches at American ports.³³ However, if his actions show an intention to remain here permanently, an alien seaman working on a U.S. vessel engaged in foreign trade can become a resident.³⁴

The term "foreign trade" includes transportation upon the high seas of passengers and freight between the United States and foreign countries.³⁵ It also includes such trade between the United States proper (including only the states, territories of Alaska and Hawaii and the District of Columbia) and other territories subject to its jurisdiction, such as Puerto Rico and the other possessions.³⁶ A vessel sailing

²⁹ John Henry Chapman, 9 TC 619.

³⁰ IRC Sec. 3797(a)(9).

³¹ Reg. 11, Secs. 29-131-2 and 29, 251-4; IT 2285, VI-1CB51, SM 5446, V-1, CB 49.

³² *Supra*, n. 12; Est. W. M. L. Fiske v. Comm., 128 F.2d 487, cert. den. 317 U.S. 635.

³³ Sec. 29, 211-3.

³⁴ Stefan Kowalski, TC Memo Dkt. No. 14939, Nov. 24, 1948.

³⁵ OD 315, CB 1, 164 (1919).

³⁶ OD 536, CB 2, 162 (1920).

via the Panama Canal from a port on the Pacific Coast to a port on the Atlantic Coast of the United States is, however, engaged in coast-side rather than foreign trade.³⁷

A seaman may also establish a residence on land within the United States the same way as any other alien. The fact that his profession requires that he be away for considerable periods of time will not, in the absence of other evidence showing an intent to change his residence, destroy his status as a resident. But residence is not acquired merely because a head tax has been paid on behalf of an alien seaman entering the United States, for the reason that the head tax is payable unless the alien who is entering the country is merely in transit through the country.³⁸ An alien seaman was held to be a non-resident alien, even though he had sought to become a citizen, because he was in this country under wartime orders of the Norwegian government.³⁹

C. PROOF OF RESIDENCE OF AN ALIEN

An alien, as has been stated before, is presumed to be a non-resident. The presumption may be overcome by proof that he has filed a declaration of intention to become a citizen, or has filed with his employer a certificate of residence on Form 1078, or by proof of other acts and statements of the alien indicative of a definite intention to acquire residence in the United States or to stay a sufficient length of time to constitute him a resident. Where the alien presents himself for determination of tax liability prior to his departure for his native country, he may overcome the presumption if he has filed a declaration of intent to become a citizen or has filed a Form 1078 within at least six months prior to the date of presentation. He may also submit proof of acts and statements showing a definite intention to acquire residence in the United States or showing that his stay in the United States has been of such an extended nature as to constitute him a resident. Whenever the proof of residence is based on other acts and statements of the alien, the internal revenue officer examining the facts may require affidavits, showing the pertinent facts, executed by credible persons, other than members of the alien's family, who have known the alien for at least six months.⁴⁰

D. LOSS OF STATUS AS A RESIDENT ALIEN

An alien who has once acquired the status of a resident does not become a non-resident until he actually departs from the United States, even though his intention to change his residence may have been formed some time before that.⁴¹ Temporary absence will not cause

³⁷ OD 784, CB 4, 116 (1921).

³⁸ *Supra*, n. 33.

³⁹ Rolf and Ruth M. Jamvold, 11 TC 122 (A).

⁴⁰ Sec. 29, 211-4.

⁴¹ Sec. 29, 211-5.

loss of status as a resident alien,⁴² and the absence may be rather protracted when there is no intention to establish a residence elsewhere.⁴³ Thus a resident alien who spent two years abroad as a soldier in the army of his native country, but who returned to this country when his enlistment was terminated, in accordance with his intention as expressed on his departure was held not to have lost his status as a resident of the United States.⁴⁴ Aliens who have established residence in the United States do not lose that status as the result of registration as enemy aliens.⁴⁵

An alien who acquires United States residence and leaves with a valid permit to re-enter, retains his status as a resident for income tax purposes as long as the re-entry permit (original or extended) is valid. This is true unless exceptional circumstances are shown, such as acts or statements that the alien has taken steps to acquire residence elsewhere, or actions showing an abandonment of residence in the United States.⁴⁶

E. DUTY OF EMPLOYER TO DETERMINE STATUS OF ALIEN EMPLOYEE

Since an employer has the duty of withholding taxes from wages paid to non-resident aliens, it is important for him to determine whether aliens in his employ are resident or non-resident. If the employee has filed a certificate claiming residence (Form 1078) or any other similar statement in writing, the employer is entitled to rely on it; or, if he is satisfied from other competent evidence in his possession that the alien is a resident, he need not withhold the tax.⁴⁷

From the viewpoint of the alien, the employer's payroll records may be useful as evidence of his, the employee's, continuous residence in the U.S. and of his status as a resident.⁴⁸

F. TRUSTS AND ESTATES

In the *B. W. Jones* case,⁴⁹ the grantors were non-resident aliens, as were the beneficiaries of the trust, and the trust was created outside the United States. In addition, most of the co-trustees were non-resident aliens. The Court nevertheless held the trust to be "a resident trust and its income taxable the same way as that of a resident individual." The fact that one of the trustees was a U.S. citizen, that the corpus was kept in the charge of that trustee, and in an office in the United States, was sufficient to enable the Court to reach this result.

⁴² OD 468, 2 CB 243 (1920).

⁴³ *Ibid.*, n. 42.

⁴⁴ *Frederico Stallforth v. Helvering*, 77 F.2d 548, cert. den. 296 U.S. 606.

⁴⁵ OD 498, 2 CB 163 (1920); OD 400, 2 CB 163 (1920).

⁴⁶ IT 4057, CB 1951-2, 93.

⁴⁷ Sec. 29, 211-6.

⁴⁸ *Ibid.*, n. 47.

⁴⁹ 46 BTA 531, aff'd 132 F.2d 914; GCM 11221, XI-1, CB 123, OD 743, 3 CB 203.

An estate, as may be gathered from the above case, is a separable taxable entity, and does not depend for its residence status upon the status of the decedent or beneficiaries, but upon the status of the trustee, executor, administrator, guardian, etc., having charge over it.⁵⁰

G. CORPORATIONS, PARTNERSHIPS AND FIDUCIARIES

An organization which constitutes a partnership or corporation according to our law can, within the meaning of the Income Tax Law, be either a foreign or domestic organization. If organized or created within the U.S. or under its law, or that of any state, the territories of Alaska and Hawaii or the District of Columbia, it is domestic in character. Otherwise, it is a foreign partnership or corporation.

A domestic corporation or partnership is automatically a resident, even though it does no business and owns no property in the United States. A foreign corporation may be a resident or non-resident. If it is engaged in a trade or business within the United States it is a resident; otherwise, it is a non-resident foreign corporation.⁵¹ Here, also, the term "United States" is used in the tax sense—that is, to exclude possessions.

An alien is engaged in United States business if he is a member of a partnership so engaged.⁵² In this respect the rule differs from the law governing trusts, which holds that a trust beneficiary⁵³ or grantor of a revocable or irrevocable trust⁵⁴ is not engaged in United States business merely because the trustee does business in the U.S.

H. DEPARTURE OF ALIENS

An alien, resident or non-resident, may not depart from the United States without procuring from a Director of Internal Revenue or District Commissioner a certificate that he has complied with his income tax obligations. If he does not present such certificate of compliance at the point of departure, he will be there examined by an internal revenue officer and taxes due will then be collected.⁵⁵ The Commissioner can also declare the taxable period immediately terminated if he finds that the taxpayer designs, by departure or otherwise, to avoid tax.⁵⁶ In such a case, any personal exemptions and credits for dependents must be prorated.⁵⁷ Credit should be given for any tax withheld.⁵⁸ Termination of the taxable period may occur each time

⁵⁰ Estate of A. F. Cooper, 9 BTA 21 (A).

⁵¹ Sec. 29, 211-6.

⁵² IRC Sec. 219; Reg. 111, Sec. 29, 219-1; Craik v. U.S., 31 F.Supp. 132; IT 3233, 1938-2, CB 192.

⁵³ Reg. 111, Sec. 29, 211-7 (C).

⁵⁴ Reg. 111, Sec. 29, 211-1 (C).

⁵⁵ IRC Sec. 146 (e) and (f); Reg. 111, Sec. 29, 146-1(b) and (c); Mimeo 2195, 21 CB 253; Spec. Rul. July 5, 1950; OD 840, 4 CB 2329; OD 385, 2 CB 243.

⁵⁶ IRC Sec. 146(a)(1).

⁵⁷ IRC Sec. 47(e).

⁵⁸ Mimeo 2195, Reg. 111, Sec. 29, 146-1(a).

the alien departs, but an annual return should subsequently be filed, and any resulting over-assessment will be refunded.⁵⁹

II. TAXABILITY OF RESIDENT ALIENS

Resident aliens are taxable generally the same as citizens of the United States. They are taxable on income derived from all sources, including sources without the U.S.,⁶⁰ and are subject to the same tax rates and administrative provisions as are our own citizens. They are entitled to the same exemptions and credits for dependents and to the same deductions.⁶¹

There is, in addition, a credit for income, war profits and excess profits taxes paid to a foreign country, but only if the foreign country of which the taxpayer is a citizen allows similar credits to citizens of the U.S. residing there.⁶² Resident aliens are required to file the same kind of tax returns as citizens of the United States, but they cannot file a joint return if either spouse was a non-resident alien at any time during the taxable year, and the splitting of income privilege is unavailable to them in such cases.⁶³

Non-resident aliens engaged in business within the United States are taxable only on income from "sources within the United States."⁶⁴

Interest on "bonds, notes or other interest bearing obligations" paid by the United States Government or by resident citizens and interest paid by resident aliens or by a domestic or resident foreign corporation, if at least 20% of the payor's gross income was derived from sources within the U.S. for the three year period ending with the close of the payor's taxable year preceding the payments, is taxable. This rule is, however, subject to income tax treaties which may exist in some cases.⁶⁵ Interest on bank deposits, open accounts, condemnation awards, insurance policies, causes of action or judgments, and U.S. tax refunds are also included as taxable income.⁶⁶ Interest paid by a domestic corporation on a security deposit, even though the deposit was made in a foreign bank and the interest was paid by a branch office in the foreign country, has been held to be includible,⁶⁷ but interest on bonds of a foreign government held in the United States and

⁵⁹ GCM 17195, XV-2 CB 107; Spec. Rul. July 5, 1950.

⁶⁰ Reg. 111, Secs. 29, 11-2 and 29, 11-1.

⁶¹ Schnur, 10 TC 208 (A).

⁶² IRC Sec. 131(a)(3); Freudman, 10 TC 775 (A); Bowring, 27 BTA 449; Wilson, 17 TC 1469; IT 3749, 1945 CB 202.

⁶³ IRC Sec. 51(b)(2).

⁶⁴ IRC Sec. 212(a); Reg. 111, Sec. 29, 212-1.

⁶⁵ IRC Sec. 119(a)(1); Reg. 111, Sec. 29, 119-2.

⁶⁶ Eitingnon, 27 BTA 1341; Waldorf Astor, 31 BTA 1009; *Helvering v. Stockholm Enskilda Bank*, 293 U.S. 84; *British Amer. Tobacco Co. v. Helvering*, 293 U.S. 95; *Comm v. Raphael*, 133 F.2d 442, cert. den. 320 U.S. 735; IT 2792, XIII-1 CB 85; IT 3216, 1938-2CB 183; GCM 13366, XIII-2 CB 164; GCM 21187, 1939-1 CB 141; GCM 21968, 1940-1 CB 67; Reg. 111, Sec. 29, 119-2.

⁶⁷ *Infra.*, n. 68.

interest received in the United States are excluded.⁶⁸ The same rule applies to interest on bonds of the International Bank.⁶⁹

Dividends paid by a U.S. corporation are includible if the corporation derived at least 20% of its gross income from sources within the United States for the three year period ending with the close of the payor's taxable year preceding the dividend declaration.⁷⁰ A distribution in redemption of stock which has the effect of a taxable dividend is taxable as a dividend.⁷¹

Dividends paid by a foreign corporation are partially includible if the corporation derived at least 50% of its gross income from sources within the U.S. for the three year period ending with the close of the payor's taxable year preceding the dividend declaration. In such a case, the portion of the dividend attributable to United States income of the declaring corporation, based upon the ratio of such income to total gross income for the three year period, is includible.⁷² The tax is not eliminated even though the dividends are paid in the foreign country by the corporation.⁷³ In this regard, however, any existing income tax treaties should be consulted.

III. COMPENSATION OF NON-RESIDENT ALIENS

Compensation paid to a non-resident alien for services rendered in the U.S. while temporarily in this country is includible in gross income.⁷⁴ Compensation for services rendered by a non-resident alien who is temporarily present in the United States for a period not in excess of 90 days during the taxable year is excluded by statute, if the aggregate amount of such compensation does not exceed \$3000 and the services are performed for a non-resident alien or foreign partnership or corporation not engaged in trade or business within the United States.⁷⁵ Compensation for services rendered outside the U.S. even though the United States Government is the employer or the employer is in the United States or is a U.S. resident, is excludible.⁷⁶ On the

⁶⁸ *Monk & Co.*, 10 TC 77; IT 3940, 1949-1 CB 113.

⁶⁹ OD 35, 1 CB 101; *Std. Marine Ins. Co.*, 4 BTA 867; *Spec. Rul. Nov. 25, 1947*; Bank Press Release No. 1108/5/48.

⁷⁰ IRC Sec. 119(a)(2)(A); Reg. 111, Sec. 29, 113-3(a).

⁷¹ *De Nobili Cigar Co.*, ITC 673, *Aff'd*, 143 F.2d 436.

⁷² IRC Sec. 119(a)(2)(B); Reg. 111, Sec. 29, 119-3(b); *Georday Enterprises, Ltd. v. Comm.*, 126 F.2d 384; *Codrington*, 6 BTA 415(A); *Ardbern Co., Ltd.*, 41 BTA 910, *rev'd on other grounds*, 120 F.2d 424; IT 1620, III-1 CB 126; *Mim.* 4323, XIV-1 CB 119; IT 2836, XIII-1 CB 81.

⁷³ *Forres*, 25 BTA 154; *Ross*, 44 BTA 1, *vacated and remanded pursuant to stipulation*.

⁷⁴ IT 3943, 1949-1 CB 83; OD 638, 3 CB 128; OD 784, 4 CB 116; OD 245, 1 CB 183.

⁷⁵ IRC Sec. 119(a)(3); Reg. 111, Sec. 29, 119-4.

⁷⁶ *Reorish*, 38 BTA 567, *aff'd* 115 F.2d 39, *cert. den.* 312 U.S. 700; *Vount*, 38 BTA 1460; *Piedras Negras Broadcasting Co.*, 43 BTA 297, *aff'd* 127 F.2d 260; *British Timken Ltd.*, 12 TC 880(A); IT 3804, 1946-1 CB 151; IT 1395, I-2 CB 229; SM 5488, V-1 CB 51.

other hand, compensation for personal services rendered in the U.S. by an agent of the non-resident is taxable.⁷⁷

Where the services are rendered partly within and partly without the United States, the compensation therefor, unless otherwise apportioned, must be apportioned on a time basis.⁷⁸

"Rentals or royalties from property located in the United States or from any interest in such property, including rentals or royalties for the use of or for the privilege of using patents, copyrights, secret processes and formulas, good will, trade marks, brands, franchises, etc., in the United States" are includible in gross income.⁷⁹ Gains, profits and income from the sale of personal property in the U.S., including stock or commodities exchanges, are also fully taxable if the personal property was previously purchased by the taxpayer, and the sale took place within the United States. The place of purchase is immaterial.⁸⁰

Subsidies received from the U.S. on export sales are United States income. Amounts received as a distribution on partial or complete liquidation of a U.S. corporation which conducted all of its business in the United States are subject to capital gains taxes, regardless of the fact that surrender of the stock and payment therefor take place in a foreign country.⁸¹

A non-resident alien's distributive share of partnership income, including so-called salary of a partner from a partnership engaged in business in the U.S., is includible to the extent that the partnership income was derived from sources in the U.S.⁸² If the non-resident alien is employed by a foreign branch of the partnership and is paid from the profits of the foreign branch, such income is not taxable.⁸³

Distributed or currently distributable income from a resident trust derived from U.S. sources is taxable to a non-resident alien benefici-

⁷⁷ *Helvering v. Bookman*, 107 F.2d 388.

⁷⁸ *Mooney*, 9 TC 713; IT 3804, 1946-1 CB 151; IT 1449, I-2 CB 152.

⁷⁹ IRC Sec. 119(a) (4); Reg. 111, Sec. 29, 119-5; *Woodhouse v. Comm.*, 337 U.S. 369; *Sabatim v. Comm.*, 98 F.2d 61, cert. den. 328 U.S. 862; *Röhmer*, 14 TC 1467(A); *Molnar*, 4 TCM 951, aff'd 156 F.2d 924; *Sanchez*, 6 TCM 1141, aff'd 162 F.2d 58, cert. den. 332 U.S. 815; *Ingram v. Bowers*, 57 F.2d 65, 932; IT 3296, 1939-2 CB 133; Reg. 111, Secs. 29, 143-2 and 29, 211-7(a).

⁸⁰ Reg. 111, Sec. 29, 212-1(b); GCM 18383, 1937-2 CB 244; IT 3137, 1937-2 CB 164; IRC Sec. 119(e); Reg. 111, Sec. 119-8; *East Coast Oil Co.*, 31 BTA 558, aff'd 85 F.2d 332, cert. den. 299 U.S. 608; *The Exelon Co.*, 45 BTA 844 (A) (1941); *Briskey Co.*, 29 BTA 987, aff'd 78 F.2d 816; GCM 25131, 1947-2 CB 85; *Kaspere Cohn Co. Ltd.*, 35 BTA 646; *Arthern Co. Ltd. v. Comm.*, 120 F.2d 424; *Hazelton Corp.*, 36 BTA 908, App. Dismissed; *Elston Co. Ltd.*, 42 BTA 208; *Stafford & Co. Inc. v. Pedrick*, 171 F.2d 42; *Cadwallader*, 13 TC 214; *R. J. Dorn & Co.*, 12 BTA 1102(A); *Amtorg Trading Corp. v. Higgins*, 150 F.2d 536.

⁸¹ *Livingston*, 4 TCM 943; GCM 13771, XIII-2 CB 229.

⁸² GCM 17255, XV-2 CB 243.

⁸³ *Ibid.*, n. 82.

ary.⁸⁴ Conversely, as to currently distributable trust income from sources outside the U.S., a non-resident alien beneficiary is not taxable.⁸⁵ But where interest on foreign bonds is not currently distributable, but is accumulated by a resident trust for future distribution to a non-resident alien, such interest is the income of the resident trust and is taxable to the trust, since the taxpayer is the resident trust or trustee and not the non-resident alien.⁸⁶ Distributed and currently distributable income from a foreign trust, derived by the trust from United States sources, is taxable to the non-resident beneficiary.⁸⁷

Income derived from a refund of tax paid in the U.S. is taxable,⁸⁸ as is income from future contracts entered into and liquidated in the United States.⁸⁹ In the latter case, however, such income is at present specifically exempted.⁹⁰ Income from discharge of a debt in the United States at less than face value is taxable.⁹¹

Gain on the liquidation of a United States corporation engaged in United States business is taxable irrespective of the place of liquidation.⁹²

Income derived from insurance received from loss of goods in transit is taxable if the goods had a situs in the U.S. at the time of loss. Situs remains at the point of shipment until a permanent situs is acquired elsewhere.⁹³

Taxes withheld must also be included as taxable income.⁹⁴

Increment on U.S. Treasury bills issued at a discount is taxable,⁹⁵ as are: (1) Income from redemption or sale in the United States of bonds purchased in the United States,⁹⁶ (2) Annuity payments,⁹⁷ (3) Damages for breach of contract to be performed in the United States,⁹⁸ (4) Damages for failure to pay interest in agreed currency, agreed to be paid by a domestic corporation,⁹⁹ (5) Amounts received for an agreement not to compete in the United States,¹⁰⁰ (6) Gain from the purchase of the Taxpayer's own obligations at a discount in the United

⁸⁴ Reg. 111, Sec. 29, 143-2; IT 3020, XV-2 CB 106; *Bence v. U.S.*, 18 F.Supp. 848;

GCM 11221, XI-2 CB 123; ARM 37, 2 CB 172; IT 1642, II-1 CB 81.

⁸⁵ IT 1642, II-1 CB 81; GCM 11221, XI-2 CB 123; ARM 37, 2 CB 172.

⁸⁶ GCM 11221, XI-2 CB 123; ARM 37, 2 CB 172; OD 743, 3 CB 203.

⁸⁷ *Bence v. U.S.*, 18 F.Supp. 848; *Mimeo*, 10 TC 307, aff'd 182 F.2d 819.

⁸⁸ *Comm. v. Suffolk Co. Ltd.*, 104 F.2d 505.

⁸⁹ *Zander & Cia Ltd.*, 42 BTA 50.

⁹⁰ IT 3137, 1937-2 CB 164; GCM 18383, 1937-2 CB 244.

⁹¹ *Corporation de Ventas de Soltre y Vodade Chile*, 44 BTA 393, rev'd on other grounds, 130 F.2d 141.

⁹² *Hay*, 2 TC 460, aff'd 145 F.2d 1001, cert. den. 324 U.S. 863.

⁹³ IT 3902, 1948-1 CB 64.

⁹⁴ IRC Sec. 143(d); Reg. 111, Sec. 29 143-9.

⁹⁵ IT 3889, 1948-1 CB 78.

⁹⁶ *Hubert de Stuers*, 26 BTA 201; *Elston Co. Ltd.*, *supra*, n. 80; IT 1398 I-2 CB 149; OD 534, 2 CB 103; OD 844, 4 CB 217; IT 2330 VI-1 CB 76.

⁹⁷ IT 2183, IV-2 CB 66; IT 2996 XV-2 CB 166.

⁹⁸ 330 AG 221, I-2 CB 192.

⁹⁹ IT 3216, 1938-2 CB 183.

¹⁰⁰ *The Korfund Co., Inc.*, 1 TC 1180.

States,¹⁰¹ (7) Alimony paid from a United States trust,¹⁰² and (8) Agricultural subsidies paid by the U.S. concerning land situated in the U.S.¹⁰³

The only exemptions allowed (except to Canadians and Mexicans) is one exemption of \$600 for the normal tax and the surtax.¹⁰⁴ In a case where a non-resident alien changes his status to that of a resident during the taxable year, he is entitled to exemptions of a resident, but not in excess of his net income for the period of residence.¹⁰⁵

Deductions are allowed for items deductible by citizens or residents, but only if and to the extent that they are connected with taxable income from sources within the United States.¹⁰⁶ Expenses, losses or other deductions must first be allocated to specific items of United States or foreign income to the extent that it is possible, and ratable apportionment is only to be used where no definite allocation can be made.¹⁰⁷ Deductions may not be allocated entirely to United States income merely because they cannot be identified as attributable to foreign income.¹⁰⁸

Interest on a debt incurred to finance an investment in foreign corporations is allocated to foreign income, even though the debt is collectible from United States assets,¹⁰⁹ as is a worthless stock loss if the stock was that of a foreign corporation.¹¹⁰

No deductions are allowed to non-residents for lodging and meals where their only business is in the U.S., merely because they maintain their home in a foreign country.¹¹¹ A taxpayer performing personal services for a short time in this country and who has his home and principal occupation in a foreign country may deduct his traveling expenses to and from the United States, as well as his traveling and lodging expenses and meals in the United States.¹¹²

Losses not connected with the taxpayer's business are deductible (whether or not connected with income from sources within the U.S.)

¹⁰¹ IT 3119, 1937-2 CB 227.

¹⁰² *Albert R. Gallatin Welsh Trust*, 16 TC 1398, *aff'd* 194 F.2d 708.

¹⁰³ IT 3216, 1938-2 CB 183.

¹⁰⁴ IRC Sec. 214; Reg. 111, Secs. 29, 214-1(b)(2); IT 3625, 1943 CB 545.

¹⁰⁵ IT 3926, 1948-2 CB 48.

¹⁰⁶ IRC Sec. 213(a); Reg. 111, Secs. 29, 119-9, 29, 213-1(b); *Stockholms Enskilda Bank*, 40 BTA 107; *Corporation de Ventas de Solitre y Yoda de Chile*, *supra*, n. 91; *DeNederlandsche Bank*, 35 BTA 53; *Std. Marine Ins. Co.*, *supra*, n. 69; *Forres*, *supra*, n. 73; *Louis Roessel & Co., Ltd.*, 2 BTA 1141; SM 4767, V-1 CB 263; IT 2028, III-1 CB 296; IT 2034, XV-2 CB 1136; GCM 26013-1949 CB 76.

¹⁰⁷ IRC Sec. 119(b) and (c); Reg. 111, Sec 29, 119-10; *DeNederlandsche Bank*, *supra*, n. 106; *Royal Ins. Co.*, 38 BTA 955; *Fajardo Sugar Co. of Puerto Rico*, 20 BTA 980.

¹⁰⁸ *Comm. v. International Std. Elec. Co.*, 144 F.2d 487, *rev'g* ITC 1153, *cert. den.* U.S. 803; *South Puerto Rico Sugar Co.*, 2 TC 738.

¹⁰⁹ *Commercial Union Ass. Co. Ltd. v. Comm.*, 144 F.2d 994.

¹¹⁰ *Comm. v. Ferro-Emanuel Corp.*, 134 F.2d 564.

¹¹¹ *Carranza*, 11 TC 224; GCM 4956, VII-2 CB 128.

¹¹² GCM 26013, 1949-2 CB 76.

if incurred in transactions entered into for profit and if such profit would have been taxable here had the transaction resulted in a profit.¹¹³ Casualty and theft losses allowable under Internal Revenue Code Section 23(e)(3) are also deductible if the loss is of property within the United States.¹¹⁴

Charitable contribution deductions are allowed whether or not connected with income from sources within the United States, but only as to contributions made to domestic corporations, community chests, vocational rehabilitation funds, or to foundations created in the U.S.¹¹⁵ Such taxpayers cannot use the optional standard deduction,¹¹⁶ but should return Form 1040B.¹¹⁷

In order to facilitate the collection of taxes from non-resident aliens, taxes are required to be withheld by persons paying out specified kinds of income from United States sources to all non-resident alien individuals, irrespective of whether the alien is engaged in United States business, and to "any partnership not engaged in trade or business in the United States and composed in whole or in part of non-resident aliens."¹¹⁸ To avoid inconvenience, a resident alien should file a certificate of residence on Form 1078 with withholding agents, who will forward it to the Commissioner of Internal Revenue, Withholding Revenue Section, with a letter of transmittal.¹¹⁹ The kinds of income are the "fixed or determinable annual or periodical" income upon which a non-resident alien not engaged in United States business is taxable.¹²⁰

"All persons in whatever capacity acting, including lessees or mortgagees of real or personal property, fiduciaries, employers and all officers and employees of the United States having the control, receipt, custody, disposal or payment" of the specified kinds of income of a non-resident alien must withhold tax.¹²¹ "When a payor corporation, or any other person (including a nominee) having the control, receipt, custody, disposal or payment of dividends has no definite knowledge of the status of a shareholder, the tax should be withheld if the shareholder's address is outside the United States. If the shareholder's address is within the United States, it may be assumed that such shareholder is a citizen or a resident thereof. Unless the name and style of the shareholder are such as to indicate clearly that he is a non-resident

¹¹³ IRC Sec. 213(b)(1).

¹¹⁴ IRC Sec. 213(b)(2).

¹¹⁵ IRC Sec. 213(c).

¹¹⁶ IRC Sec. 213(d).

¹¹⁷ Reg. 111, Sec. 29, 217-2(b).

¹¹⁸ IRC Sec. 143(b); Reg. 111, Sec. 29, 143-1(a); *Brushaber v. Union Pacific R.R.*, 240 U.S. 1 (1915).

¹¹⁹ Reg. 111, Sec. 29, 143-3.

¹²⁰ IRC Sec. 143(b); Reg. 111, Sec. 29, 143-2.

¹²¹ IRC Secs. 143 and 3707(a)(16); Reg. 111, Sec. 29, 143(a).

alien, an address in care of another person in the United States does not of itself warrant the treating of the shareholder as a non-resident alien. If a shareholder changes his address from a place without the United States to a place within the United States, the tax should be withheld unless proof is furnished showing that he is a citizen or resident of the United States. A person's written statement that he is a citizen or resident of the United States may be relied on by the payor of income as proof that such person is a citizen or resident of the United States."¹²²

The following payors must withhold tax:

(1) A resident owner of record of stock if the beneficial owner is a non-resident alien.¹²³

(2) A husband who receives community income for his non-resident alien wife.¹²⁴

(3) A manager for a foreign syndicate.¹²⁵

(4) One who pays income to a resident trustee for non-resident aliens.¹²⁶

(5) Resident or domestic fiduciaries. These are required to deduct the income tax at the source from all fixed or determinable annual or periodical gains, profits and income of non-resident alien beneficiaries to the extent that such items constitute gross income from sources within the United States.¹²⁷ This does not apply to distributed or distributable gains.¹²⁸

(6) One who pays income to a non-resident alien fiduciary though the beneficiaries are all U.S. citizens or residents.¹²⁹

(7) A trustee of a trust created by a non-resident alien individual if the income is taxable to the grantor because the trust falls within the definition of revocable trust under Internal Revenue Code Section 167, even though the trust beneficiaries are U.S. citizens or residents.¹³⁰

(8) One who deposits income in a non-resident alien's bank account.¹³¹

(9) One who makes payment to a U.S. agent of a non-resident alien; if he does not withhold, the agent must.¹³²

¹²² Reg. 111, Sec. 29, 144-2.

¹²³ IT 2938, XIV-2 CB 139; IT 2997, XV-2 CB 106.

¹²⁴ IT 3889, *supra*, n. 95.

¹²⁵ Van Iderstine, 24 BTA 291.

¹²⁶ *Ibid.* n. 125.

¹²⁷ St. Francis Hospital, 42 BTA 1004, *aff'd* 125 F.2d 553, cert. den. 316 U.S. 697; OD 1085, 5 CB 191; Reg. 111, Sec. 29, 143-1(a).

¹²⁸ IT 3945, 1941-2 CB 195.

¹²⁹ Reg. 111, Sec. 29, 143-1(a).

¹³⁰ *Ibid.* n. 129.

¹³¹ IT 2624, XI-1 CB 122; OD 330, 1 CB 239; Mimeo 5075, 1940-2 CB 141; Spec. Rul. Jan. 20, 1942.

¹³² IT 2624, *Ibid.*, n. 131; GCM 4683, VII-2 CB 69.

(10) One who pays rent to a non-resident alien.¹³³

(11) A corporation which makes a distribution other than a non-taxable distribution payable in stock or stock rights or a distribution in partial or complete liquidation, without regard to any claim that all or a portion of such distribution is not taxable.¹³⁴ But where stock is owned jointly by a non-resident alien and a U.S. citizen or resident, the corporation need only withhold on the portion of a dividend to which the alien is entitled.¹³⁵

(12) An assignee of the property of a debtor, where such assignee assumed the obligations of the debtor. Such taxes must be withheld as were required to be withheld by the debtor.¹³⁶

The following payors need not withhold:

(1) One who promises or guarantees, but makes no actual payments to an alien.¹³⁷ Payment in kind, however, may not be made by a payor to the non-resident alien until the payor is placed in funds for the withholding of cash.¹³⁸

(2) A person who pays accrued interest to a non-resident alien upon the sale of a bond between interest dates.¹³⁹

(3) A person who makes payments to a U.S. partnership despite the fact that a non-resident alien is a partner.¹⁴⁰ A contrary rule prevails if the partnership is not engaged in United States business.¹⁴¹

(4) A debtor corporation which appoints a withholding agent and files notice of such appointment with the Commissioner of Internal Revenue.¹⁴²

(5) A bank upon which checks are drawn.¹⁴³ The maker of the check is deemed to have made the payment.¹⁴⁴

(6) The issuing corporation or its warrant agent when outstanding stock warrants are sold.¹⁴⁵

(7) The owner of a mine leased to an independent contractor where the latter employs a non-resident alien.¹⁴⁶

(8) A partnership with respect to a distribution by it to a non-resident alien partner.¹⁴⁷

¹³³ GCM 18835.

¹³⁴ Reg. 111, Sec. 29, 143-1(a); IT 3020.

¹³⁵ IT 3053, 1937-1 CB 110.

¹³⁶ Reg. 111, Sec. 29, 143-1(a).

¹³⁷ *Tonopah and Tidewater R.R. Co. Ltd. v. Comm.*, 112 F.2d 970, overruling IT 3059, 1937-1 CB 111; Brunch, *supra*.

¹³⁸ Reg. 111, Sec. 29, 143-7.

¹³⁹ Reg. 111, Sec. 29, 143-1.

¹⁴⁰ IRC Sec. 143(b); IT 3233, 1938-2 CB 192.

¹⁴¹ IRC Sec. 143(b).

¹⁴² Reg. 111, Secs. 29, 143-1(a) and 29, 143-7.

¹⁴³ IT 3020, XV-2 CB 106.

¹⁴⁴ IT 3535, 1942-1 CB 129.

¹⁴⁵ Spec. Rul. April 21, 1949.

¹⁴⁶ OD 175, 1 CB 182.

¹⁴⁷ GCM 2467, III-2 CB 188, modified in other respects by GCM 8594, IX-2 CB 354.

The kinds of income subject to withholding are limited to the "fixed or determinable annual or periodical" United States income upon which a non-resident alien, not engaged in United States business, is taxable.¹⁴⁸ This form of withholding is not required with respect to compensation for personal services of a Canadian or Mexican resident who enters and leaves the U.S. at frequent intervals, or with respect to wages for the agricultural labors of any other non-resident alien who frequently enters and leaves the United States.¹⁴⁹

No withholding is required with respect to the distributable capital gains of a trust,¹⁵⁰ nor in the case of dividends paid by a foreign corporation unless the corporation is engaged in United States business and more than 85% of its gross income for the three year period ending with the close of its taxable year preceding the declaration of such dividend was derived from United States sources.¹⁵¹ In this regard, existing income tax treaties should be consulted.

The withholding rate is 30% of gross income without deductions or exemptions, except where modified by income tax treaties.¹⁵² (The proper rate of exchange where income is paid in foreign currency is discussed in the *International Sleeping Car Co.* case.¹⁵³) The withholding agent must withhold at the tax rate prevailing at the time payment is made by him to the non-resident alien, irrespective of when the income was earned.¹⁵⁴

Return and payment is required of the payor-withholding agent on March 15th, and such withholding agent is personally liable for the tax.¹⁵⁵ Payment of the tax by the recipient of the income relieves the agent of liability, however.¹⁵⁶ On the other hand, the withholding agent is not freed of his duty to withhold merely because the recipient has posted a bond to insure payment of the tax,¹⁵⁷ or has an agent here who will file a return for him,¹⁵⁸ or because the recipient claims no tax is due.¹⁵⁹

With respect to most kinds of income, the payor must file Form 1042.¹⁶⁰ In the case of interest on bonds or other obligations of corporations, the payor must file an annual return on Form 1012 on the

¹⁴⁸ IRC Sec. 143(b); Reg. 111, Sec. 29, 143-2.

¹⁴⁹ Reg. 111, Sec. 29, 143-3; IT 3590, 1942-2 CB 147.

¹⁵⁰ IT 3495, *supra*; IT 3781, *supra*.

¹⁵¹ IRC Sec. 143(b).

¹⁵² *Ibid.*, n. 151; Reg. 111, Sec. 29, 144-2.

¹⁵³ 14 BTA 702; OD 700, 3 CB 214.

¹⁵⁴ IT 3020, XV-2 CB 106; IT 2798, XIII-2 CB 90; OD 167, 1 CB 182.

¹⁵⁵ IRC Sec. 143(c), as amended by Rev. Act of 1950; Reg. 111, Sec. 29, 143-7.

¹⁵⁶ IRC Sec. 143(c); Reg. 111, Sec. 29, 143-9.

¹⁵⁷ IT 1357, I-1 CB 223.

¹⁵⁸ OD 1087, 5 CB 193; OD 958, 4 CB 111.

¹⁵⁹ IT 3020, XV-2 CB 106.

¹⁶⁰ Reg. 111, Sec. 29, 143-7.

last day of the month following termination of the quarter, accompanied by Form 1001.¹⁶¹

Withheld tax is credited against the liability shown on the non-resident alien's return. If the withheld tax exceeds the tax liability, the non-resident alien or his agent is entitled to and should claim credit or refund.¹⁶² The withholding agent is entitled to obtain a refund of an overpayment only if the tax was not actually withheld by it, but was paid out of its own funds.¹⁶³ He can, however, contest liability.¹⁶⁴ As between the withholding agent and the non-resident alien, the liability for tax is primarily upon the latter. Hence, if the withholding agent has paid the tax out of its own funds, it should be able to recover the amount from the non-resident alien.¹⁶⁵ If, before the withholding agent has turned over withheld funds to the United States Government, it discovers that there has been an improper withholding, it may restore the amount to the non-resident alien.¹⁶⁶

It is again emphasized that frequent reference should be made to existing Income Tax Treaties and Treasury Regulations under such treaties for provisions regarding interchange of information between the United States and other contracting countries and for additional information returns which may be required of withholding agents.

IV. CHANGES IN INCOME, ESTATE AND GIFT TAX PROVISIONS AFFECTING ALIENS UNDER THE NEW 1954 INTERNAL REVENUE CODE

No major changes in the income tax treatment of aliens have been made. Aliens continue to be divided into the categories of resident aliens, non-resident aliens engaged in business within the United States and non-resident aliens not so engaged. The last category is further divided into those having United States gross income of up to \$15,400 and those having in excess of this figure. No attempt was made in the new Code to define "residence," nor to define "engaged in trade or business within the United States."

As before resident aliens are generally taxable the same as U.S. citizens: that is, on income from all sources including sources without the United States. Non-resident aliens continue to be taxable only on income from sources within this country.

A few provisions were made, however, in the particular provisions dealing with non-resident aliens.

¹⁶¹ *Ibid.* n. 160.

¹⁶² IRC Sec. 143(e), 143(f) and 216; Reg. 111, Sec. 29, 143-9 and 29, 217-2.

¹⁶³ IRC Sec. 143(f); *Bank of America Nat. Trust & Savings Assoc. v. Anglim*, 138 F.2d 7; *Pauker v. U.S.*, 23 F.Supp. 821; *Capitol Estates, Inc.*, 46 BTA 986, *aff'd* 138 F.2d 156.

¹⁶⁴ Spec. Rul. April 18, 1947.

¹⁶⁵ *McGrath v. Dravo Corp.*, 183 F.2d 709; *A. Gasmer, Inc. v. McGrath*, 94 F.Supp. 724.

¹⁶⁶ *Supra*, n. 164.

Section 871 enlarges the tax base of non-resident alien individuals not engaged in business within the U.S. to include certain gains, profits and income which are considered gains from the sale or exchange of capital assets. The change does not affect gains from the sale or exchange of capital assets such as stocks and securities, but only those gains *considered* to be gains from the sale of capital assets. It would, for example, affect the gain of a non-resident alien individual, not engaged in business within the United States, who received within one year all distributions payable to him from an exempt pension trust on account of his separation from service with his employer, which gain, under the new Code Section 402(a)(2), would be considered to be a gain from the sale or exchange of a capital asset held for more than six months.

Sections 631(b) and (c) and 1231 relate to the gains from the disposal of timber and coal.

Section 1235 relates to gains derived from the transfer of an interest in a patent.

Section 861(a)(3) and 871 broaden the old Code's provisions for exclusion from gross income of compensation for services performed by a non-resident alien present in the U.S. for a period not in excess of 90 days during the taxable year, where the aggregate compensation does not exceed \$3000 and the services were performed for a foreign employer. Under the new sections, the exemption is extended to cases where services are performed for a foreign branch of a domestic employer.

Trusts and Estates: Subchapter J of Chapter 1 of the Code includes specific provisions with respect to the taxation of non-resident alien beneficiaries on distributed and currently distributable income from an estate or trust. It largely codifies existing case law.

Sections 652(b), 661(b) and 662(b) adopt the prevailing judicial and administrative view that estates and trusts are only conduits through which income flows to its beneficiaries, except where income is accumulated by the estate or trust for future distribution. The distributed and distributable income from estates and trusts is expressly declared to have the same character in the hands of the beneficiary as in the hands of the estate or trust. Unless the terms of the instrument specifically allocate different classes of income to particular beneficiaries, the amounts distributed or distributable are to be treated as consisting of the same proportion of each class of items entering into the computation of distributed or distributable net income of the estate or trust as the total of each class bears to the total distributed or distributable net income of the estate or trust. Accordingly, in the case of a resident estate or trust, the distributed or currently distribu-

table income derived from sources without the United States would not be taxable to a non-resident alien beneficiary.

In the case of a foreign estate or trust, the distributed or currently distributable estate or trust income (Section 643(a)(6)) derived by the trust from sources within the United States would be taxable to the non-resident alien beneficiary if he would be taxable on income of such class from United States sources had he received it directly without the interposition of an estate or trust. But the non-resident alien beneficiary would not be taxable on the distributed or currently distributable estate or trust income derived by the trust from sources without the U.S.

Sections 2(a) and 6013(a)(1): As under the old Code, the benefit of income splitting between spouses (with consequent reduction in tax rate) available to citizens and resident aliens, is not extended to non-resident aliens; nor are they permitted to file joint returns. The benefit of full income splitting has now been provided to a qualifying surviving spouse for the first two years after the death of the deceased spouse. This privilege is similarly denied non-resident aliens. As under the old Code, the somewhat reduced tax rate which is provided in the case of an unmarried individual who cannot qualify for full income splitting, but who qualifies as "head of the household" (new Code Section 1(b)) is not available to a non-resident alien.

Sections 871(a), 116(d) and 34(e): Both the dividend exclusion and the credit for dividends received are available to resident alien individuals who are subject to the regular individual income tax, but not to those whose tax is computed at the flat 30% rate on gross income.

Section 37(h) is another novel provision of general application, providing a limited exemption, by means of a tax credit, to all forms of retirement income. This new Section is inapplicable to non-resident alien individuals.

Section 1441 requires a withholding agent to deduct and withhold tax in the case of a non-resident alien individual or partnership falling within its terms in the amounts described in Section 402(a)(2), Section 631(b) and (c) and Section 1235, which are considered to be gains from the sale or exchange of capital assets. It provides further that if the amount of such gain is not known to the withholding agent, he shall deduct and withhold such amount, not exceeding 30% of the proceeds from such sale or exchange, as may be necessary to assure that the tax deducted and withheld shall not be less than 30% of such gain.

Section 1442, in the case of foreign corporations, requires a withholding agent to also deduct and withhold a tax of 30% on amounts described in Section 631(b) and (c), which are considered gains from

the sale or exchange of capital assets. This statute automatically makes applicable the qualification of Section 1441 that if the amount of such gain is not known to the withholding agent, he shall deduct and withhold such amount, not exceeding 30% of the proceeds from such sale or exchange, as may be necessary to assure that the tax deducted and withheld is not less than 30% of such gain.

Sections 1361 and 1361(b)(3) present a novel proposition in the new Code, which gives partnerships and proprietorships possessing certain qualifications the right to be taxed as corporations. The section is not applicable to a partnership or proprietorship if any partner or proprietor is a non-resident alien or foreign entity.

Section 6851 continues the power in the Secretary of the Treasury to terminate the taxable year of an alien departing from the U.S. The new provision permits the taxable year, once closed by the Secretary, to be reopened. This result was accomplished prior to the new Code by administrative ruling.

Section 7456(b) states that if the Tax Court requires any petitioner, being a non-resident alien individual, foreign trust or estate or foreign corporation, to produce in court any books or records which are relevant to the issues in the case and are in the possession or control of the petitioner or any parent or subsidiary corporation or any other entity controlled by or controlling the petitioner, and if such required books or records are not produced or made available for inspection or copying within a reasonable time, the Tax Court shall upon motion strike out the pleadings or parts thereof, or render judgment by default.

Section 6316 provides that the Secretary of the Treasury, at his discretion, may permit the payment of taxes in currency of foreign countries.

Foreign Corporations and the Income Tax: No major changes in the income tax treatment have been made. All foreign corporations continue to be taxable only on income from sources within the United States. They continue to be divided into those engaged in trade or business within the United States (resident foreign corporations) and those not so engaged. No attempt was made in the new Code to define the term, "engaged in trade or business within the United States," as applied to corporations.

As before, resident foreign corporations are subject to income tax at the normal tax and surtax rates upon all income derived from sources within the United States. Non-resident foreign corporations are subject to income tax only on "fixed or determinable annual or periodical" income derived from sources within the United States, the tax being at the uniform rate of 30% without deductions or credits, in the absence of contrary income tax treaty provisions. Few substantive

changes were made in the particular provisions dealing with foreign corporations.

Section 881, which deals with the tax on non-resident foreign corporations, contains no reference to treaties. It enlarges the tax base of non-resident foreign corporations to include amounts which are *considered* gains from the sale or exchange of capital assets, but only those covered by the new Code Sections 631(b) and (c), relating to gains derived from the disposal of timber or coal respectively.

Code Sections 34 and 116 do not apply to dividends paid by foreign corporations.

Under Section 532(b), as before, resident and non-resident foreign corporations may be subject to the accumulated earnings tax.

Part II of Subchapter G (Sections 541-547) allows a foreign corporation, whether resident or non-resident, to be either a "personal holding company" or a "foreign personal holding company" subject to the tax imposed by Part III (Sections 551-557).

Section 552 provides for an exemption from the foreign personal holding company tax with respect to certain corporations organized and doing business under the banking act of a foreign country, if the Secretary of the Treasury or his delegate finds that the corporations were not organized or availed of for the purpose of evading or avoiding U.S. income taxes on their shareholders.

Section 556 defines "undistributed foreign personal holding company income."

Section 342 retains the special short-term capital gain treatment, previously prescribed by the last sentence of old Code Section 115(c), with respect to gain realized by a shareholder upon liquidation of certain foreign personal holding companies. The rigorous requirement of monthly and other information returns by officers, directors and 50% of the shareholders of such companies is retained without material change in new Code Section 6035.

Section 367 is derived from and corresponds in function to Section 112(i) of the old Code, in defeating the tax avoidance purpose of a transfer to a foreign corporation having as one of its principal objectives the avoidance of U.S. income tax on previously unrealized appreciation in capital assets. This section, like its predecessor, removes the application to such a transfer of those provisions of the Code which might otherwise limit or eliminate the recognition of gain on such transfer. The special excise tax on such transfers which are made to avoid income tax previously imposed by old Code Sections 1251-1254 is retained in the new Code Sections 1491-1494 (Chapter 5, Section A).

Section 6046 retains with no material change the old Code's provisions with respect to special information returns as to the formation or reorganization of foreign corporations. The time for filing such

returns is to be prescribed by regulations under new Code Section 6071.

Estate and Gift Taxes: Subtitle B of the new Code imposes the estate and gift taxes. Chapter 11 (Sections 2001-2007) imposes the estate tax, Chapter 12 (Sections 2501-2524), the gift tax.

As before, for estate and gift tax purposes, aliens are divided into the two main categories of residents and non-residents. No definitions have been supplied as to these terms. Resident aliens continue to be subject to estate and gift tax in the same manner as citizens. The resident alien is taxable not only on property situated in the United States, but also on property situated outside this country, except that the estate tax never extends to real property outside the United States.

Subchapter B (Sections 2101-2106) of Chapter 11 contains the estate tax provisions applicable to estates of non-resident aliens. The tax on such persons is imposed upon the transfer of only the portion of the estate that was situated within the United States. Particular rules for determining the *situs* of property have been laid down in some estate tax treaties. The new Code contains no provisions concerning the determination of situs of property except a provision treating the situs of stocks; namely, Section 2104, which retains the rule that stock in a domestic corporation is deemed to be situated in the United States, irrespective of where the certificates are physically located. This Section does change the rule with regard to stock in a foreign corporation. Such stock cannot be deemed to be property within the United States even if the certificates are physically located here.

Section 2102 continues the credits against estate tax for state death taxes, gift tax, and estate tax on prior transfers, but contains a change from prior law in that it gives no credit for state death taxes where the value of the property does not exceed \$40,000.

Section 6091 provides for the fixing by regulations of the place for filing estate tax returns of non-resident aliens.

Section 7851(a)(2)(A) provides that the estate tax provisions of the new Code are applicable with respect to the estates of decedents dying after the date of its enactment.

Section 2501 subdivides non-resident aliens into those engaged in business in the United States and those not so engaged. This new Section provides that in the case of non-resident aliens engaged in business in the United States, a gift tax is imposed with respect to gifts of property (tangible or intangible) situated in the United States. In the case of non-resident aliens not so engaged, the gift tax is imposed only with respect to tangible property situated in the United States.

Section 2511(b) parallels the change in the estate tax made by new Code Section 2104 with regard to the situs of stock.

The gift tax provisions of the new Code are applicable with respect to the calendar year 1955 and all subsequent calendar years under new Code Section 7851(a)(2)(B).