

104TH CONGRESS  
2D SESSION

# S. 1942

To amend the Internal Revenue Code of 1986 to provide tax treatment for foreign investment through a United States regulated investment company comparable to the tax treatment for direct foreign investment and investment through a foreign mutual fund.

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## IN THE SENATE OF THE UNITED STATES

JULY 10, 1996

Mr. BAUCUS (for himself, Mr. GORTON, and Mrs. MURRAY) introduced the following bill; which was read twice and referred to the Committee on Finance

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## A BILL

To amend the Internal Revenue Code of 1986 to provide tax treatment for foreign investment through a United States regulated investment company comparable to the tax treatment for direct foreign investment and investment through a foreign mutual fund.

1       *Be it enacted by the Senate and House of Representa-*  
2       *tives of the United States of America in Congress assembled,*

3       **SECTION 1. SHORT TITLE.**

4       (a) SHORT TITLE.—This Act may be cited as the  
5       “Investment Competitiveness Act of 1996”.

6       (b) AMENDMENT OF 1986 CODE.—Whenever in this  
7       Act an amendment or repeal is expressed in terms of an

1 amendment to, or repeal of, a section or other provision,  
2 the reference shall be considered to be made to a section  
3 or other provision of the Internal Revenue Code of 1986.

4 **SEC. 2. TREATMENT OF CERTAIN DIVIDENDS OF REGU-**  
5 **LATED INVESTMENT COMPANIES.**

6 (a) TREATMENT OF CERTAIN DIVIDENDS.—

7 (1) NONRESIDENT ALIEN INDIVIDUALS.—Sec-  
8 tion 871 (relating to tax on nonresident alien indi-  
9 viduals) is amended by redesignating subsection (k)  
10 as subsection (l) and by inserting after subsection (j)  
11 the following new subsection:

12 “(k) EXEMPTION FOR CERTAIN DIVIDENDS OF REG-  
13 ULATED INVESTMENT COMPANIES.—

14 “(1) INTEREST-RELATED DIVIDENDS.—

15 “(A) IN GENERAL.—Except as provided in  
16 subparagraph (B), no tax shall be imposed  
17 under paragraph (1)(A) of subsection (a) on  
18 any interest-related dividend received from a  
19 regulated investment company.

20 “(B) EXCEPTIONS.—Subparagraph (A)  
21 shall not apply—

22 “(i) to any interest-related dividend  
23 received from a regulated investment com-  
24 pany by a person to the extent such divi-  
25 dend is attributable to interest (other than

1 interest described in subparagraph (E) (i)  
2 or (iii)) received by such company on in-  
3 debtedness issued by such person or by any  
4 corporation or partnership with respect to  
5 which such person is a 10-percent share-  
6 holder,

7 “(ii) to any interest-related dividend  
8 with respect to stock of a regulated invest-  
9 ment company unless the person who  
10 would otherwise be required to deduct and  
11 withhold tax from such dividend under  
12 chapter 3 receives a statement (which  
13 meets requirements similar to the require-  
14 ments of subsection (h)(5)) that the bene-  
15 ficial owner of such stock is not a United  
16 States person, and

17 “(iii) to any interest-related dividend  
18 paid to any person within a foreign coun-  
19 try (or any interest-related dividend pay-  
20 ment addressed to, or for the account of,  
21 persons within such foreign country) dur-  
22 ing any period described in subsection  
23 (h)(6) with respect to such country.

24 Clause (iii) shall not apply to any dividend with  
25 respect to any stock which was acquired on or

1 before the date of the publication of the Sec-  
2 retary's determination under subsection (h)(6).

3 “(C) INTEREST-RELATED DIVIDEND.—For  
4 purposes of this paragraph, an interest-related  
5 dividend is any dividend (or part thereof) which  
6 is designated by the regulated investment com-  
7 pany as an interest-related dividend in a writ-  
8 ten notice mailed to its shareholders not later  
9 than 60 days after the close of its taxable year.  
10 If the aggregate amount so designated with re-  
11 spect to a taxable year of the company (includ-  
12 ing amounts so designated with respect to divi-  
13 dends paid after the close of the taxable year  
14 described in section 855) is greater than the  
15 qualified net interest income of the company for  
16 such taxable year, the portion of each distribu-  
17 tion which shall be an interest-related dividend  
18 shall be only that portion of the amounts so  
19 designated which such qualified net interest in-  
20 come bears to the aggregate amount so des-  
21 ignated.

22 “(D) QUALIFIED NET INTEREST IN-  
23 COME.—For purposes of subparagraph (C), the  
24 term ‘qualified net interest income’ means the  
25 qualified interest income of the regulated in-

1 vestment company reduced by the deductions  
2 properly allocable to such income.

3 “(E) QUALIFIED INTEREST INCOME.—For  
4 purposes of subparagraph (D), the term ‘quali-  
5 fied interest income’ means the sum of the fol-  
6 lowing amounts derived by the regulated invest-  
7 ment company from sources within the United  
8 States:

9 “(i) Any amount includible in gross  
10 income as original issue discount (within  
11 the meaning of section 1273) on an obliga-  
12 tion payable 183 days or less from the date  
13 of original issue (without regard to the pe-  
14 riod held by the company).

15 “(ii) Any interest includible in gross  
16 income (including amounts recognized as  
17 ordinary income in respect of original issue  
18 discount or market discount or acquisition  
19 discount under part V of subchapter P and  
20 such other amounts as regulations may  
21 provide) on an obligation which is in reg-  
22 istered form; except that this clause shall  
23 not apply to—

24 “(I) any interest on an obligation  
25 issued by a corporation or partnership

1 if the regulated investment company  
2 is a 10-percent shareholder in such  
3 corporation or partnership, and

4 “(II) any interest which is treat-  
5 ed as not being portfolio interest  
6 under the rules of subsection (h)(4).

7 “(iii) Any interest referred to in sub-  
8 section (i)(2)(A) (without regard to the  
9 trade or business of the regulated invest-  
10 ment company).

11 “(F) 10-PERCENT SHAREHOLDER.—For  
12 purposes of this paragraph, the term ‘10-per-  
13 cent shareholder’ has the meaning given to such  
14 term by subsection (h)(3)(B).

15 “(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—

16 “(A) IN GENERAL.—Except as provided in  
17 subparagraph (B), no tax shall be imposed  
18 under paragraph (1)(A) of subsection (a) on  
19 any short-term capital gain dividend received  
20 from a regulated investment company.

21 “(B) EXCEPTION FOR ALIENS TAXABLE  
22 UNDER SUBSECTION (a)(2).—Subparagraph (A)  
23 shall not apply in the case of any nonresident  
24 alien individual subject to tax under subsection  
25 (a)(2).

1           “(C) SHORT-TERM CAPITAL GAIN DIVI-  
2           DEND.—For purposes of this paragraph, a  
3           short-term capital gain dividend is any dividend  
4           (or part thereof) which is designated by the reg-  
5           ulated investment company as a short-term cap-  
6           ital gain dividend in a written notice mailed to  
7           its shareholders not later than 60 days after the  
8           close of its taxable year. If the aggregate  
9           amount so designated with respect to a taxable  
10          year of the company (including amounts so des-  
11          ignated with respect to dividends paid after the  
12          close of the taxable year described in section  
13          855) is greater than the qualified short-term  
14          gain of the company for such taxable year, the  
15          portion of each distribution which shall be a  
16          short-term capital gain dividend shall be only  
17          that portion of the amounts so designated  
18          which such qualified short-term gain bears to  
19          the aggregate amount so designated.

20          “(D) QUALIFIED SHORT-TERM GAIN.—For  
21          purposes of subparagraph (C), the term ‘quali-  
22          fied short-term gain’ means the excess of the  
23          net short-term capital gain of the regulated in-  
24          vestment company for the taxable year over the  
25          net long-term capital loss (if any) of such com-

1           pany for such taxable year. For purposes of this  
2           subparagraph, the excess of the net short-term  
3           capital gain for a taxable year over the net  
4           long-term capital loss for a taxable year (to  
5           which an election under section 4982(e)(4) does  
6           not apply) shall be determined without regard  
7           to any net capital loss or net short-term capital  
8           loss attributable to transactions after October  
9           31 of such year, and any such net capital loss  
10          or net short-term capital loss shall be treated as  
11          arising on the 1st day of the next taxable year.  
12          To the extent provided in regulations, the pre-  
13          ceding sentence shall apply also for purposes of  
14          computing the taxable income of the regulated  
15          investment company.”.

16           (2) FOREIGN CORPORATIONS.—Section 881 is  
17          amended by redesignating subsection (e) as sub-  
18          section (f) and by inserting after subsection (d) the  
19          following new subsection:

20           “(e) TAX NOT TO APPLY TO CERTAIN DIVIDENDS  
21          OF REGULATED INVESTMENT COMPANIES.—

22           “(1) INTEREST-RELATED DIVIDENDS.—

23           “(A) IN GENERAL.—Except as provided in  
24          subparagraph (B), no tax shall be imposed  
25          under paragraph (1) of subsection (a) on any

1 interest-related dividend (as defined in section  
2 871(k)(1)) received from a regulated investment  
3 company.

4 “(B) EXCEPTION.—Subparagraph (A)  
5 shall not apply—

6 “(i) to any dividend referred to in sec-  
7 tion 871(k)(1)(B), and

8 “(ii) to any interest-related dividend  
9 received by a controlled foreign corporation  
10 (within the meaning of section 957(a)) to  
11 the extent such dividend is attributable to  
12 interest received by the regulated invest-  
13 ment company from a person who is a re-  
14 lated person (within the meaning of section  
15 864(d)(4)) with respect to such controlled  
16 foreign corporation.

17 “(C) TREATMENT OF DIVIDENDS RE-  
18 CEIVED BY CONTROLLED FOREIGN CORPORA-  
19 TIONS.—The rules of subsection (c)(5)(A) shall  
20 apply to any interest-related dividend received  
21 by a controlled foreign corporation (within the  
22 meaning of section 957(a)) to the extent such  
23 dividend is attributable to interest received by  
24 the regulated investment company which is de-  
25 scribed in clause (ii) of section 871(k)(1)(E)

1 (and not described in clause (i) or (iii) of such  
2 section).

3 “(2) SHORT-TERM CAPITAL GAIN DIVIDENDS.—  
4 No tax shall be imposed under paragraph (1) of sub-  
5 section (a) on any short-term capital gain dividend  
6 (as defined in section 871(k)(2)) received from a  
7 regulated investment company.”.

8 (3) WITHHOLDING TAXES.—

9 (A) Subsection (c) of section 1441 is  
10 amended by adding at the end thereof the fol-  
11 lowing new paragraph:

12 “(12) CERTAIN DIVIDENDS RECEIVED FROM  
13 REGULATED INVESTMENT COMPANIES.—

14 “(A) IN GENERAL.—No tax shall be re-  
15 quired to be deducted and withheld under sub-  
16 section (a) from any amount exempt from the  
17 tax imposed by section 871(a)(1)(A) by reason  
18 of section 871(k).

19 “(B) SPECIAL RULE.—For purposes of  
20 subparagraph (A), clause (i) of section  
21 871(k)(1)(B) shall not apply to any dividend  
22 unless the regulated investment company knows  
23 that such dividend is a dividend referred to in  
24 such clause. A similar rule shall apply with re-

1 spect to the exception contained in section  
2 871(k)(2)(B).”.

3 (B) Subsection (a) of section 1442 is  
4 amended—

5 (i) by striking “and the reference in  
6 section 1441(c)(10)” and inserting “the  
7 reference in section 1441(c)(10)”, and

8 (ii) by inserting before the period at  
9 the end thereof the following: “, and the  
10 references in section 1441(c)(12) to sec-  
11 tions 871(a) and 871(k) shall be treated as  
12 referring to sections 881(a) and 881(e)  
13 (except that for purposes of applying sub-  
14 paragraph (A) of section 1441(c)(12), as  
15 so modified, clause (ii) of section  
16 881(e)(1)(B) shall not apply to any divi-  
17 dend unless the regulated investment com-  
18 pany knows that such dividend is a divi-  
19 dend referred to in such clause)”.

20 (b) ESTATE TAX TREATMENT OF INTEREST IN CER-  
21 TAIN REGULATED INVESTMENT COMPANIES.—Section  
22 2105 (relating to property without the United States for  
23 estate tax purposes) is amended by adding at the end  
24 thereof the following new subsection:

25 “(d) STOCK IN A RIC.—

1           “(1) IN GENERAL.—For purposes of this sub-  
2 chapter, stock in a regulated investment company  
3 (as defined in section 851) owned by a nonresident  
4 not a citizen of the United States shall not be  
5 deemed property within the United States in the  
6 proportion that, at the end of the quarter of such in-  
7 vestment company’s taxable year immediately pre-  
8 ceding a decedent’s date of death (or at such other  
9 time as the Secretary may designate in regulations),  
10 the assets of the investment company that were  
11 qualifying assets with respect to the decedent bore  
12 to the total assets of the investment company.

13           “(2) QUALIFYING ASSETS.—For purposes of  
14 this subsection, qualifying assets with respect to a  
15 decedent are assets that, if owned directly by the de-  
16 cedent, would have been—

17                   “(A) amounts, deposits, or debt obligations  
18 described in subsection (b) of this section,

19                   “(B) debt obligations described in the last  
20 sentence of section 2104(c), or

21                   “(C) other property not within the United  
22 States.”.

23           (c) TREATMENT OF REGULATED INVESTMENT COM-  
24 PANIES UNDER SECTION 897.—

1           (1) Paragraph (1) of section 897(h) is amended  
2           by striking “REIT” each place it appears and in-  
3           serting “qualified investment entity”.

4           (2) Paragraphs (2) and (3) of section 897(h)  
5           are amended to read as follows:

6           “(2) SALE OF STOCK IN DOMESTICALLY-CON-  
7           TROLLED ENTITY NOT TAXED.—The term ‘United  
8           States real property interest’ does not include any  
9           interest in a domestically-controlled qualified invest-  
10          ment entity.

11          “(3) DISTRIBUTIONS BY DOMESTICALLY-CON-  
12          TROLLED QUALIFIED INVESTMENT ENTITIES.—In  
13          the case of a domestically-controlled qualified invest-  
14          ment entity, rules similar to the rules of subsection  
15          (d) shall apply to the foreign ownership percentage  
16          of any gain.”.

17          (3) Subparagraphs (A) and (B) of section  
18          897(h)(4) are amended to read as follows:

19          “(A) QUALIFIED INVESTMENT ENTITY.—  
20          The term ‘qualified investment entity’ means  
21          any real estate investment trust and any regu-  
22          lated investment company.

23          “(B) DOMESTICALLY-CONTROLLED.—The  
24          term ‘domestically-controlled qualified invest-  
25          ment entity’ means any qualified investment en-

1           tity in which at all times during the testing pe-  
2           riod less than 50 percent in value of the stock  
3           was held directly or indirectly by foreign per-  
4           sons.”.

5           (4) Subparagraphs (C) and (D) of section  
6           897(h)(4) are each amended by striking “REIT”  
7           and inserting “qualified investment entity”.

8           (5) The subsection heading for subsection (h) of  
9           section 897 is amended by striking “REITS” and  
10          inserting “CERTAIN INVESTMENT ENTITIES”.

11          (d) EFFECTIVE DATE.—

12           (1) IN GENERAL.—Except as otherwise pro-  
13          vided in this subsection, the amendments made by  
14          this section shall apply to dividends with respect to  
15          taxable years of regulated investment companies be-  
16          ginning after the date of the enactment of this Act.

17           (2) ESTATE TAX TREATMENT.—The amend-  
18          ment made by subsection (b) shall apply to estates  
19          of decedents dying after the date of the enactment  
20          of this Act.

21           (3) CERTAIN OTHER PROVISIONS.—The amend-  
22          ments made by subsection (c) (other than paragraph  
23          (1) thereof) shall take effect on the date of the en-  
24          actment of this Act.

○