

105TH CONGRESS  
1ST SESSION

# S. 815

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

MAY 23, 1997

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 1997”.

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 “(iv) Any interest-related dividend in-  
12 cludable in gross income with respect to  
13 stock of another regulated investment com-  
14 pany.

15 “(F) 10-PERCENT SHAREHOLDER.—For  
16 purposes of this paragraph, the term ‘10-per-  
17 cent shareholder’ has the meaning given such  
18 term by subsection (h)(3)(B).

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

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

1           “(B) EXCEPTION FOR ALIENS TAXABLE  
2 UNDER SUBSECTION (a)(2).—Subparagraph (A)  
3 shall not apply in the case of any nonresident  
4 alien individual subject to tax under subsection  
5 (a)(2).

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

1           “(D) QUALIFIED SHORT-TERM GAIN.—For  
2 purposes of subparagraph (C), the term ‘quali-  
3 fied short-term gain’ means the excess of the  
4 net short-term capital gain of the regulated in-  
5 vestment company for the taxable year over the  
6 net long-term capital loss (if any) of such com-  
7 pany for such taxable year. For purposes of this  
8 subparagraph—

9           “(i) the net short-term capital gain of  
10 the regulated investment company shall be  
11 computed by treating any short-term cap-  
12 ital gain dividend includible in gross in-  
13 come with respect to stock of another regu-  
14 lated investment company as a short-term  
15 capital gain, and

16           “(ii) the excess of the net short-term  
17 capital gain for a taxable year over the net  
18 long-term capital loss for a taxable year (to  
19 which an election under section 4982(e)(4)  
20 does not apply) shall be determined with-  
21 out regard to any net capital loss or net  
22 short-term capital loss attributable to  
23 transactions after October 31 of such year,  
24 and any such net capital loss or net short-

1 term capital loss shall be treated as arising  
2 on the 1st day of the next taxable year.

3 To the extent provided in regulations, clause  
4 (ii) shall apply also for purposes of computing  
5 the taxable income of the regulated investment  
6 company.”

7 (2) FOREIGN CORPORATIONS.—Section 881 is  
8 amended by redesignating subsection (e) as sub-  
9 section (f) and by inserting after subsection (d) the  
10 following new subsection:

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

13 “(1) INTEREST-RELATED DIVIDENDS.—

14 “(A) IN GENERAL.—Except as provided in  
15 subparagraph (B), no tax shall be imposed  
16 under paragraph (1) of subsection (a) on any  
17 interest-related dividend (as defined in section  
18 871(k)(1)) received from a regulated investment  
19 company.

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

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

24 “(ii) to any interest-related dividend  
25 received by a controlled foreign corporation

1 (within the meaning of section 957(a)) to  
2 the extent such dividend is attributable to  
3 interest received by the regulated invest-  
4 ment company from a person who is a re-  
5 lated person (within the meaning of section  
6 864(d)(4)) with respect to such controlled  
7 foreign corporation.

8 “(C) TREATMENT OF DIVIDENDS RE-  
9 CEIVED BY CONTROLLED FOREIGN CORPORA-  
10 TIONS.—The rules of subsection (c)(5)(A) shall  
11 apply to any interest-related dividend received  
12 by a controlled foreign corporation (within the  
13 meaning of section 957(a)) to the extent such  
14 dividend is attributable to interest received by  
15 the regulated investment company which is de-  
16 scribed in clause (ii) of section 871(k)(1)(E)  
17 (and not described in clause (i) or (iii) of such  
18 section).

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

24 (3) WITHHOLDING TAXES.—

1           (A) Subsection (c) of section 1441 is  
2 amended by adding at the end the following  
3 new paragraph:

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

6           “(A) IN GENERAL.—No tax shall be re-  
7 quired to be deducted and withheld under sub-  
8 section (a) from any amount exempt from the  
9 tax imposed by section 871(a)(1)(A) by reason  
10 of section 871(k).

11           “(B) SPECIAL RULE.—For purposes of  
12 subparagraph (A), clause (i) of section  
13 871(k)(1)(B) shall not apply to any dividend  
14 unless the regulated investment company knows  
15 that such dividend is a dividend referred to in  
16 such clause. A similar rule shall apply with re-  
17 spect to the exception contained in section  
18 871(k)(2)(B).”

19           (B) Subsection (a) of section 1442 is  
20 amended—

21           (i) by striking “and the reference in  
22 section 1441(c)(10)” and inserting “the  
23 reference in section 1441(c)(10)”, and

24           (ii) by inserting before the period at  
25 the end the following: “, and the references

1 in section 1441(c)(12) to sections 871(a)  
2 and 871(k) shall be treated as referring to  
3 sections 881(a) and 881(e) (except that for  
4 purposes of applying subparagraph (A) of  
5 section 1441(c)(12), as so modified, clause  
6 (ii) of section 881(e)(1)(B) shall not apply  
7 to any dividend unless the regulated invest-  
8 ment company knows that such dividend is  
9 a dividend referred to in such clause)”.  
10

11 (b) ESTATE TAX TREATMENT OF INTEREST IN CER-  
12 TAIN REGULATED INVESTMENT COMPANIES.—Section  
13 2105 (relating to property without the United States for  
14 estate tax purposes) is amended by adding at the end the  
15 following new subsection:

16 “(d) STOCK IN A RIC.—

17 “(1) IN GENERAL.—For purposes of this sub-  
18 chapter, stock in a regulated investment company  
19 (as defined in section 851) owned by a nonresident  
20 not a citizen of the United States shall not be  
21 deemed property within the United States in the  
22 proportion that, at the end of the quarter of such in-  
23 vestment company’s taxable year immediately pre-  
24 ceding a decedent’s date of death (or at such other  
25 time as the Secretary may designate in regulations),  
the assets of the investment company that were

1 qualifying assets with respect to the decedent bore  
2 to the total assets of the investment company.

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

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

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

11 “(C) other property not within the United  
12 States.”

13 (c) TREATMENT OF REGULATED INVESTMENT COM-  
14 PANIES UNDER SECTION 897.—

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

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

20 “(2) SALE OF STOCK IN DOMESTICALLY-CON-  
21 TROLLED ENTITY NOT TAXED.—The term ‘United  
22 States real property interest’ does not include any  
23 interest in a domestically-controlled qualified invest-  
24 ment entity.

1           “(3) DISTRIBUTIONS BY DOMESTICALLY-CON-  
2 TROLLED QUALIFIED INVESTMENT ENTITIES.—In  
3 the case of a domestically-controlled qualified invest-  
4 ment entity, rules similar to the rules of subsection  
5 (d) shall apply to the foreign ownership percentage  
6 of any gain.”

7           (3) Subparagraphs (A) and (B) of section  
8 897(h)(4) are amended to read as follows:

9           “(A) QUALIFIED INVESTMENT ENTITY.—

10           The term ‘qualified investment entity’ means  
11           any real estate investment trust and any regu-  
12           lated investment company.

13           “(B) DOMESTICALLY-CONTROLLED.—The

14           term ‘domestically-controlled qualified invest-  
15           ment entity’ means any qualified investment en-  
16           tity in which at all times during the testing pe-  
17           riod less than 50 percent in value of the stock  
18           was held directly or indirectly by foreign per-  
19           sons.”

20           (4) Subparagraphs (C) and (D) of section  
21 897(h)(4) are each amended by striking “REIT”  
22 and inserting “qualified investment entity”.

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

1 (d) EFFECTIVE DATE.—

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

7 (2) ESTATE TAX TREATMENT.—The amend-  
8 ment made by subsection (b) shall apply to estates  
9 of decedents dying after the date of the enactment  
10 of this Act.

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

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