Honorable John Sparkman
Chairman, Committee on Banking,
Housing and Urban Affairs
United States Senate
Washington, D.C. 20510

Honorable Russell B. Long
Chairman, Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am enclosing two copies of a memorandum outlining legislative proposals enabling the creation of Foreign Portfolio Sales Corporations (or Trusts) to be organized in the United States for the sale of mutual fund shares to foreigners. The memorandum was prepared jointly by members of the staffs of the Commission and the Treasury Department and discusses proposed amendments to the Investment Company Act and to the Internal Revenue Code. The proposals were developed by an inter-agency Offshore Funds Task Force, comprised of representatives of the Commission, the Treasury Department, the State Department and the Federal Reserve Board. The Task Force was assembled on the initiative of the Commission as a follow-up to recommendations in the Institutional Investor Study submitted to the Congress by the Commission in March 1971.

In the Institutional Investor Study, the Commission, in a chapter on Offshore Mutual Funds, stated that:

In the present climate of concern fostered by the well publicized difficulties experienced by certain offshore funds and their sponsors, the Commission believes that foreign investor confidence in offshore funds that invest in American securities could be bolstered significantly if they were to become subject to Commission regulation under federal securities laws. Offshore funds currently receive treatment under the Internal Revenue Code which provides them with competitive advantages over domestic, registered investment companies seeking to sell in offshore markets. Equalization of these advantages would enable U.S. registered investment
companies to compete more effectively with unregulated offshore funds. The net result would be beneficial both to foreign investor protection and the United States securities markets, as well as to the United States balance of payments.

Accordingly, the Commission recommended that ". . . a high level governmental task force be organized to explore and develop the possibility of the establishment and regulation of Foreign Portfolio Sales Corporations as well as registered offshore investment companies. We would expect such a task force to consider appropriate tax treatment for such funds and nonresident foreign investors . . . "

The basic role of the Task Force was to formulate a program by which existing or new offshore funds could be attracted on shore so that the full protection of the federal securities laws would be available. The Task Force concluded that such funds could be attracted to the United States if they could retain the tax benefits afforded by the Foreign Investors Tax Act of 1966, which relaxed United States taxation of foreign direct investors in the United States to encourage additional investment. One effect of that legislation, together with existing tax law, was to permit the incorporation of unregulated investment companies in foreign countries with low or non-existent income taxes as a conduit for foreign investors in the United States, offering foreign investors the following tax treatment through investment in foreign mutual funds:

(1) No United States capital gains tax is applicable to sales of the fund's portfolio of United States securities or to the investor's sale or redemption of shares in the mutual fund itself. The fund is also free to engage in short-term trading without United States tax consequences.

(2) No United States estate taxes are applicable, since the United States portfolio is owned by a foreign corporation.

(3) It is possible to accumulate income in the fund without distribution to the shareholders (which might subject them to local taxes). The income of the fund from the United States in the form of dividends and interest is ordinarily subject to a 30 percent United States withholding tax. The distribution of income to foreigners by the fund is not subject to any additional United States tax.
Task Force reviewed existing United States laws and consulted formally with a Business Advisory Group. The Task Force generally agreed on the outline of a proposal for a Foreign Portfolio Sales Corporation (FPSC) as a new form of United States mutual fund, organized in the United States, registered with the Commission but intended for sale only to nonresidents and noncitizens of the United States. The attached memorandum describes the proposals in greater detail.

Under these proposals legislation would be sought:

(1) To amend the Investment Company Act of 1940 to add a new section 7(a)(1) to provide specifically for the registration and regulation of domestic investment companies organized for the sale of their securities to foreigners, together with related amendments to provide greater flexibility under sections 7(d) and 7(e)(2) to the Commission in allowing registration of foreign investment companies and to enable the Commission to deal with the problem of "shell" companies organized in the United States with foreign officers, directors, and trustees. (A preliminary draft of this legislation is enclosed.) We recommend that Congress consider this portion of the proposed legislation initially.

(2) If Congress considers the regulatory portion of the proposed legislation favorably, we recommend that it consider amending the Internal Revenue Code of 1954 to provide that United States mutual funds which register with the Commission can sell their shares exclusively to foreign investors with tax benefits comparable to those available to offshore funds under the 1966 Act described above. Among the more important aspects would be exemption from tax at the corporate level on capital gains (foreign investors, including offshore funds, already have this exemption); no tax on the FPSC on dividends and interest from foreign securities held in the fund's portfolio (however, not more than 25 percent of the FPSC's total portfolio can be in foreign securities); if the IET is extended in 1973, it would not apply to foreign securities purchased by the FPSC. The FPSC would be allowed (a) to elect to pay a 30 percent tax on dividends and interest at the corporate level in lieu of a United States withholding tax (i.e., the shareholders would not have any tax formalities to deal with); or (b) withhold at a 30 percent or lower tax treaty rate, on distributions to their shareholders. If the FPSC were selling only in tax-treaty countries where a 15 percent reduced withholding rate applies, the 30 percent corporate or withholding tax could be reduced to 15 percent.
The Code would also be amended to provide an exemption for the shareholders of the FPSC from the estate tax (as is the case for foreign investors in an offshore fund). (A preliminary draft of this legislation is also enclosed together with a table showing in summary form the present and proposed United States tax treatment of foreign shareholders of domestic and offshore mutual funds.)

The Commission believes that the increased investor protection afforded to foreigners by the proposal would result in a desirable improvement of foreign investor confidence in offshore funds investing in United States securities. The facts alleged in the Commission's recent complaint in SEC v. Robert L. VESCO, et al., indicate the extent of the current regulatory void and how important it may be in terms of investor protection and the preservation of the integrity of the United States securities markets to take whatever steps may be possible to fill that void.

At the same time, the Commission understands that the Treasury Department anticipates that there would be only a minimal revenue loss, if any, from this proposal. Offshore funds now provide an investment vehicle for foreign investors with which these new funds would be competitive. The proposal merely permits the domestication of such funds without changing the basic tax effect on the fund or the foreign shareholders. Indeed, increased United States investment through these funds may well generate additional revenue through increased economic activity.

The Office of Management and Budget has advised that there is no objection to the submission of this proposed legislation from the standpoint of the Administration's program.

Sincerely yours,

G. Bradford Cook
Chairman

Enclosures

Similar letters to: Congressmen Staggers, Hills, Moss,
Senators Williams, Roth, Saxbe and Brooke
Description of
Foreign Portfolio Sales Corporation Proposal (FPSC)

I. General Description

A special category of corporation would be recognized under a new section of the Internal Revenue Code of 1954 and under the Investment Company Act of 1940. In general, the new entity would be required to be organized and operated as follows:

1. The FPSC would be a corporation incorporated under the laws of any of the States of the United States or the District of Columbia (or a trust as described in V. below).

2. The FPSC must be registered under the Investment Company Act of 1940 and be in compliance with the regulations of the Securities and Exchange Commission. The corporation would generally be subject to the same S.E.C. rules and regulations as domestically owned investment companies, including registration under the Securities Act of its securities. In order to qualify for registration under the Investment Company Act, the FPSC would be required to have more than 100 shareholders or make a public offering of its shares.
(3) Except through the stage of organization and prior to public sale, there would be no United States shareholders. The FPSC would not be permitted to sell its shares to citizens or residents of the U.S., and if such persons acquired shares there would be provision for automatic redemption.

(4) Unsolicited sales of shares to foreigners temporarily in the United States (i.e., nonresidents) would not be prohibited.

(5) The FPSC would have only one class of stock.

(6) The limitations on the income and portfolio of a regulated investment company under section 851(b) of the Internal Revenue Code would be applicable to the FPSC.

(7) United States margin requirements would be applicable to portfolio acquisitions by the FPSC on the same basis as registered domestic funds. Such margin requirements would also be applicable to sales of FPSC securities made in the United States to foreigners temporarily in the United States, i.e., non-residents.

(8) No more than 25 percent of the FPSC's portfolio could be invested in foreign stock or securities. The test would be applied on the basis of the fair market value of stock or securities carried in the FPSC's portfolio. Stock or securities issued by foreign finance subsidiaries
U. S. companies (or by domestic finance subsidiaries in order to raise capital for use outside the United States) would be considered foreign stock or securities. This would also mean that interest paid on obligations issued by a foreign or domestic finance subsidiary would not be subject to tax in the hands of the FPSC. See II(A)(3), infra.

The FPSC would be permitted to engage in the following activities:

(1) The FPSC could issue registered shares or arrange for bearer depository receipts for its shares (as is a common practice in European markets). Appropriate procedures would be established for depositing the shares or receipts for voting and the exercise of other rights.

(2) The FPSC would not be required to maintain its principal office outside the United States as offshore mutual funds are presently required to do in order to obtain favorable U. S. tax treatment. Accordingly, the restrictions contained in the present Treasury Regulations would not be applicable to the FPSC and it would have much greater centralization of control over its operations, records, etc.
(3) The acquisition of foreign securities by the FPSC would not be subject to the Federal Reserve Voluntary Foreign Credit Restraint Program.

II. Tax Treatment of FPSC and its Shareholders

A new section of the Internal Revenue Code would provide the following tax treatment for a corporation (or trust, see V infra) meeting the above requirements. In general, these provisions would approximate the tax treatment presently enjoyed by offshore funds with respect to the income taxation of the corporation and its foreign shareholders, estate and gift taxation, and the Interest Equalization Tax.

A. Taxation of Corporation

(1) Capital gain on sales of U. S. or foreign stock or securities would not be subject to tax regardless of the length of time the FPSC held such stock or securities. This is presently the treatment of capital gains of a nonresident alien or foreign corporation (including an offshore fund) on investments held directly in U. S. securities.
(2) Dividends and interest received by the FPSC with respect to U. S. stock or securities would be subject to a 30 percent tax on the net amount of such income. However, the FPSC would be given an election to distribute its dividend and interest income annually in which case there would be no tax at the corporate level, but a 30 percent withholding tax (or lower tax treaty rate where applicable) would apply to the actual amount of such distributions. Consideration will also be given to the possibility of providing for a 15 percent rate at the corporate level where there is an accumulation fund and the FPSC is selling exclusively in treaty countries.

(3) Dividends and interest received by the FPSC with respect to foreign stock or securities within the 25 percent foreign portfolio limit would not be subject to tax.

(4) Other income received by the FPSC would be subject to a 30 percent tax on a net basis.*

(5) The accumulated earnings tax would not apply to the corporation.

*Under Internal Revenue Code section 851(b)(2), a regulated investment company is permitted to have up to 10 percent of its gross income from sources other than dividends, interest and capital gain.
(6) If the IET is extended in 1973, it would not apply to acquisitions of foreign stock or securities by the FPSC after the date of extension.

B. Taxation of Foreign Shareholders

(1) There would be no withholding tax on distributions by the FPSC to its shareholders unless the corporation makes the election referred to in A(2), supra., in which case distributions of dividends and interest received by the FPSC with respect to U. S. stock or securities would be subject to a 30 percent withholding tax or lower treaty rate depending on the residence of the foreign shareholder.

(2) Under currently applicable tax rules, there would be no capital gains tax on sales of shares in the FPSC by its foreign shareholders or on the redemption of such shares unless the foreign shareholder was present in the U. S. for 183 days during the year in which the sale or redemption took place and the sale or redemption occurred in the United States.

(3) There would be no U. S. estate or gift taxes applicable to shares of the FPSC owned by foreign shareholders.
III. S.E.C. Regulation of FPSC

(1) It is proposed that the Investment Company Act be amended to add a new section 7(e)(1) to specifically provide for the registration and regulation of domestic investment companies organized for the sale of their securities to foreigners.

(2) A related amendment would provide greater flexibility under section 7(d) to the Commission in allowing registration of foreign investment companies. This should better enable the Commission to administer the Act in light of developments in foreign securities regulation and recent adoption of an OECD Code of proposed uniform standards for the regulation of investment companies.

(3) It is also proposed that a new section 7(e)(2) be added to the Act to enable the Commission to deal with the problem of "shell" companies organized in the United States with foreign officers, directors, and trustees. Proposed section 7(e)(2) would provide regulatory authority with respect to consent to service of process and other enforcement tools.
N. Federal Reserve Board Considerations

(1) An exemption would be provided for the FPSC so that the acquisition of foreign securities by it would not be subject to the Voluntary Foreign Credit Restraint Program.

(2) United States margin requirements would be applicable to portfolio acquisitions by the FPSC on the same basis as registered domestic funds. Such margin requirements would also be applicable to sales of FPSC securities made in the United States to foreigners temporarily in the United States, i.e., non-residents.

V. General Description of Foreign Unit Investment Trust

Under existing practice, shares of U.S. registered mutual funds are often sold to domestic and foreign investors through a unit investment trust. The unit investment trust takes title to the shares of a single registered mutual fund and the investors acquire corresponding interests in the trust. Prior to 1969, these unit investment trusts were treated for tax purposes as a separate taxable corporation. However, in 1969, the Internal Revenue Code was amended* to provide that unit investment trusts which register with the S.E.C. and issue periodic payment plan certificates are not treated as separate taxable entities. Instead, each holder of an interest in the trust is treated as owning a proportionate share of the assets of the trust, i.e., the shares of the underlying fund.

* Section 851(f)
In the case of unit investment trusts selling to foreigners, the tax law already offers many of the tax benefits available to foreigners purchasing shares in an offshore mutual fund. However, the U. S. estate tax is applicable to foreign decedents owning an interest in a unit investment trust created by a U. S. mutual fund, and would not be imposed on shares in an offshore mutual fund. Accordingly, to provide the equivalent tax treatment as presently enjoyed by offshore funds, it is proposed to amend the Code to exempt foreigners from the estate tax with respect to shares in U. S. registered mutual funds which are acquired through a unit investment trust selling exclusively to foreign investors. (Foreign Unit Investment Trust.)*

Related amendments would provide substantially the same tax treatment as proposed for the FPSC. For example, capital gains distributions received by the trust from the underlying fund could be reinvested in the fund without the imposition of a U. S. capital gains tax. Distributions of dividends and interest received by the trust would be subject to a 30 percent withholding tax or lower treaty rate depending on the country of residence of the holders of the interests.

*A further amendment would be necessary to allow Foreign Unit Investment Trusts to sell interests to foreigners on a basis other than a periodic payment plan as presently required by section 851(f)(1)(A).
in the trust. The one principal difference between the FPSC and the Foreign Unit Investment Trust concerns purchases of foreign stock or securities by the underlying mutual fund. In the case of a mutual fund sold to foreigners through a Foreign Unit Investment Trust, purchases of foreign stock or securities could be made by the underlying fund without regard to the 25 percent limit applicable to a FPSC, but the Federal Reserve Voluntary Foreign Credit Restraint Program would apply instead. Moreover, it would not be possible to extend an IET exemption to purchases of foreign stock or securities by the underlying fund. Finally, dividends and interest received by the underlying fund from foreign stock or securities would be subject to U.S. withholding tax when distributed to the trust.

It is anticipated that Foreign Unit Investment Trusts will be used primarily by established U.S. mutual funds not wishing to incur the expense of organizing and registering a FPSC, and by funds seeking to use their record of past earnings to facilitate sales of their shares abroad. However, there will be no reason why a newly organized U.S. registered mutual fund could not use a foreign unit investment trust rather than a FPSC.
A BILL

To amend the Investment Company Act of 1940 to provide for the registration and regulation of domestic investment companies organized for the sale of their securities to foreigners.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, that this Act may be cited as the Foreign Portfolio Sales Corporation Act of 1973.

Sec. 2. The Investment Company Act of 1940 is amended as follows:

(1) Section 7(d) thereof is amended to read as follows:

"7(d) No investment company, unless organized or otherwise created under the laws of the United States or of a State, and no depositor or trustee of or underwriter for such a company not so organized or created, shall make use of the mails or any means or instrumentality of interstate commerce, directly or indirectly, to offer for sale, sell, or deliver after sale, in connection with a public offering any security of which such company is the issuer. Notwithstanding the provisions of this subsection and of Section 8(a), the Commission is authorized, upon application by an investment company organized or otherwise created under the laws of a foreign country, to issue a conditional or unconditional order permitting such company to register under this title and to make a public offering of its securities by use of the mails and means or instrumentalities of interstate commerce, if the Commission finds that, by reason of special circumstances or arrangements, it is both legally and practically feasible effectively to enforce the provisions of this title against
such company and that the issuance of such order is otherwise
consistent with the public interest and the protection of investors.
In considering any such application, the Commission may take into account
the differing laws, regulations, customs and business conditions of
particular countries in which such companies are organized and the
adequacy of existing regulation in such countries."

(2) Section 7 of the Investment Company Act is further amended
by adding a new subsection (e) to read as follows:

"(e)(1) In addition to the requirements of Section 7(a), no
investment company organized under the laws of any State which limits
the offer and sale of its securities to persons who are not citizens
or residents of the United States shall use the mails or any means or
instrumentality of interstate commerce directly or indirectly in
connection with its business in contravention of such rules and
regulations or orders as the Commission may prescribe as necessary
and appropriate in the public interest or for the protection of
investors to assure that it is both legally and practically feasible
effectively to enforce the provisions of this title. In considering
such rules, regulations or orders, or rules, regulations or orders adopted
under any other section of this title, the Commission may take into account
the differing laws, regulations, customs and business conditions of particular
countries in which such company may offer or sell its securities and the
adequacy of existing regulation in such countries."
"(e)(2) In addition to the requirements of Section 7(a), no investment company organized under the laws of any State and having any officer, director or trustee who is not a resident of the United States, nor any depositor or trustee of or underwriter for such company, shall make use of the mails or any means or instrumentality of interstate commerce, directly or indirectly, in connection with its business in contravention of such rules and regulations or orders as the Commission may prescribe as necessary and appropriate in the public interest or for the protection of investors to assure that it is both legally and practically feasible effectively to enforce the provisions of this title. In considering such rules, regulations or orders, or rules, regulations or orders adopted under any other section of this title, the Commission may take into account the differing laws, regulations, customs and business conditions of any country in which such officer, director or trustee resides or in which such company may offer or sell its securities and the adequacy of existing regulation in such countries."
A BILL

To amend the Internal Revenue Code of 1954 to provide tax treatment for foreign portfolio sales corporations regulated by the Securities and Exchange Commission.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

That Subchapter M of chapter 1 (relating to regulated investment companies and real estate investment trusts) is amended by adding at the end thereof the following new part:

"PART III - FOREIGN PORTFOLIO SALES CORPORATIONS

"Sec. 859. Definition of a foreign portfolio sales corporation.
"Sec. 860. Taxation of a foreign portfolio sales corporation and its shareholders.

"Sec. 859. DEFINITION OF A FOREIGN PORTFOLIO SALES CORPORATION.

(a) GENERAL RULE.--For purposes of this subtitle, the term "foreign portfolio sales corporation" means any domestic corporation (other than a personal holding company as defined in section 542) which, at all times during the taxable year --

(1) is registered under the Investment Company Act of 1940, as amended (54 Stat. 789; 15 U.S.C. 80 a-1 to 80 b-2), either as a management company or as a unit investment trust,
(2) does not have more than one class of stock outstanding,

(3) does not offer its stock in the United States or to any United States person as defined in section 7701(a)(30),

(4) does not have any shareholder who is a United States person as defined in section 7701(a)(30), except under the conditions set forth in regulations prescribed by the Secretary or his delegate,

(5) meets the requirements of subsection (b).

(b) LIMITATIONS.—A corporation shall not be considered to be a foreign portfolio sales corporation for its taxable year unless --

(1) it elects to be a foreign portfolio sales corporation,

(2) it meets the requirements of paragraphs (2), (3) and (4) of section 851(b), and

(3) not more than 25% of the value of its total assets is represented, at any time during the taxable year, by stock of foreign issuers, debt obligations of foreign obligors, or both.

(c) ELECTION BY CORPORATION.

(1) An election under subsection (b) shall be made in such manner as the Secretary or his delegate may prescribe by regulations.
(2) An election under subsection (b) shall be effective for the taxable year of the corporation for which it is made and for all succeeding taxable years of the corporation, until it is terminated with respect to a taxable year.

(d) CERTAIN UNIT INVESTMENT TRUSTS -- Notwithstanding section 851(f)(1), if a unit investment trust described in section 851(f)(1) (which need not issue periodic payment plan certificates) meets the election and other requirements of subsections (a) and (b) for the taxable year, such trust shall be treated as a domestic corporation qualifying as a foreign portfolio sales corporation. In applying this subsection, the terms "stock" and "shareholder" as used in subsection (a) shall mean "an interest in a unit investment trust" and "a holder of an interest in a unit investment trust", respectively."
Sec. 860. TAXATION OF A FOREIGN PORTFOLIO SALES CORPORATION AND ITS SHAREHOLDERS.

(a) TAXATION OF CORPORATION.--

(1) IMPOSITION OF TAX ON INVESTMENT COMPANY TAXABLE INCOME.--There is hereby imposed, subject to the election provided under subsection (c), for each taxable year upon the investment company taxable income of a foreign portfolio sales corporation a tax of 30%. The tax payable under this subsection shall be in lieu of the normal tax and surtax provided in section 11.

(2) INVESTMENT COMPANY TAXABLE INCOME.--The investment company taxable income shall be the taxable income of the foreign portfolio sales corporation adjusted as follows:

(A) There shall be excluded the excess, if any, of capital gains over capital losses.

(B) There shall be excluded the foreign source income of the corporation derived from stock of a foreign issuer or a debt obligation of a foreign obligor.

(C) The net operating loss deduction provided in section 172 shall not be allowed.
(D) The deductions for corporations provided in Part VIII (except section 248) in subchapter B (sections 241 and following, relating to the deduction for dividends received, etc.) shall not be allowed.

(3) CAPITAL GAINS.-- The excess, if any, of capital gains of a foreign portfolio sales corporation over its capital losses shall not be subject to tax.

(b) TAXATION OF SHAREHOLDERS.-- The shareholders of a foreign portfolio sales corporation shall not be subject to tax under section 871(a)(1)(A) or 881(a)(1) on distributions of earnings and profits received from such corporation which are attributable to its capital gains, attributable to its foreign source income described in section 860(a)(2)(B), or attributable to its investment company taxable income for a taxable year for which an election under subsection (c) was not in effect.

(c) ELECTION BY FOREIGN PORTFOLIO SALES CORPORATION.

(1) IN GENERAL. -- If a foreign portfolio sales corporation --
(A) distributes all of its earnings and profits attributable to its investment company taxable income for a taxable year within the period ending 60 days after the close of such taxable year, and

(B) provides written notice to its shareholders within the period specified in subparagraph (A) of the amount of each shareholder's distribution,

the foreign portfolio sales corporation may elect for such taxable year not to be subject to the tax on its investment company taxable income imposed by subsection (a)(1).

(2) MANNER OF MAKING ELECTION AND NOTIFYING SHAREHOLDERS.--The election provided in and the notice to shareholders required by paragraph (1) shall be made in such manner as the Secretary of the Treasury or his delegate may prescribe by regulations.

(3) YEARS FOR WHICH EFFECTIVE.--An election under paragraph (1) shall be effective only for the taxable year of the foreign portfolio sales corporation for which it is made.

(4) EFFECT OF ELECTION ON SHAREHOLDERS.--Notwithstanding subsection (b), if a foreign portfolio sales corporation makes the election provided in paragraph (1), each shareholder of such foreign portfolio sales corporation shall be taxed in
accordance with section 871 or 881 on distributions by the corporation not attributable to capital gains or foreign source income described in section 860(a)(2)(B)."

Sec. 2. Section 1441(c) (relating to withholding of tax) is amended by adding at the end thereof the following:

"(9) DISTRIBUTIONS FROM FOREIGN PORTFOLIO SALES CORPORATIONS.--No deduction or withholding under subsection (a) shall be required in the case of a distribution from a foreign portfolio sales corporation which distribution is not taxable to the shareholder under section 860(b). A taxable distribution from a foreign portfolio sales corporation will be treated as a dividend and will be subject to withholding under subsection (a)."
Sec. 3. Section 532(b) (relating to accumulated earnings tax) is amended by striking out paragraphs (2) and (3) thereof and by adding at the end thereof the following:

"(2) a foreign personal holding company (as defined in section 552),

(3) a corporation exempt from tax under subchapter F (section 501 and following), or

(4) a foreign portfolio sales corporation (as defined in section 859)."
Sec. 4. Section 2105 is amended by adding at the end thereof the following:

"(d) STOCK IN A FOREIGN PORTFOLIO SALES CORPORATION.--For purposes of this subchapter, stock in a foreign portfolio sales corporation (as defined in section 859) owned and held by a nonresident not a citizen of the United States shall not be deemed property within the United States."
Sec. 5. The amendments made by this Act shall apply with respect to taxable years beginning after December 31, 1972.
<table>
<thead>
<tr>
<th></th>
<th>Domestic Registered Fund (No Change Proposed)</th>
<th>Offshore Fund (No Change Proposed)</th>
<th>Proposed FPSC</th>
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<tbody>
<tr>
<td>1. Capital gains - Corporate level</td>
<td>No tax on sales of portfolio securities if subchapter M. requirements followed.</td>
<td>No tax on sales of portfolio securities</td>
<td>Same</td>
</tr>
<tr>
<td>2. Capital gains - shareholder</td>
<td>No tax on sales or redemption of fund shares</td>
<td>No tax on sales or redemption of fund shares</td>
<td>Same</td>
</tr>
<tr>
<td>3. Income tax - corporate level</td>
<td>No tax if Subchapter M requirements followed</td>
<td>U.S. source dividends and interest ordinarily subject to 30% withholding, except that for Netherlands Antilles companies no withholding on interest and 15% withholding on dividends, if fund elects to be taxed as corporation for local law purposes (N.A. local law tax is 23% on net interest income and 15% on dividends).</td>
<td>U.S. source dividends and interest subject to withholding at 30% or lower tax treaty rate on distributions to shareholders. Not more than 25% of total portfolio could be in foreign securities (if IET extended it would not apply to FPSC purchases). However, FPSC could elect to pay 30% tax at corporate level in lieu of withholding tax on shareholders.**/ This would not reduce net amount of U.S. tax receipts - it would only mean the taxes would be paid by FPSC rather than by FPSC shareholders.</td>
</tr>
<tr>
<td>4. Income tax - shareholder</td>
<td>30% withholding **/</td>
<td>None on distribution because of withholding in 3 above</td>
<td>See 3 above</td>
</tr>
<tr>
<td>5. Estate tax</td>
<td>Subject to tax</td>
<td>None, because foreign corporation</td>
<td>None</td>
</tr>
</tbody>
</table>

**/ Domestic shareholder pays tax at individual rates

**/ Although not in present draft, Treasury staff contemplates that 30% corporate tax could be reduced to 15% if FPSC selling only in tax treaty countries.