Jan Casimir Lewenhaupt

20 T.C. 151 (1953)

Samuel Taylor, Esq., and Walter G. Schwartz, Esq., for the petitioner. Leonard A. Marcussen, Esq., for the respondent.

The Commissioner has determined a deficiency in income tax for the year 1946 in the amount of $33,820.30. The petitioner contests the entire deficiency and claims overpayment of tax in the amount of $4,345.95. He was a citizen and resident of Sweden during and before the taxable year.

The deficiency results principally from the inclusion in the petitioner's gross income of a long-term capital gain in the amount of $152,555.87, realized upon the sale of real property located in the United States. Petitioner claims that the capital gain is not taxable. Other adjustments made by the Commissioner have been settled by the stipulation of the parties which will be given effect under Rule 50.

The issues presented for decision are:

(1) Whether the provisions of article IX of the tax convention between the United States and Sweden are applicable to a capital [pg. 152]gain derived from the sale in 1946 of real property situated in the United States by a citizen and resident of Sweden.

(2) If the first issue is decided for the respondent, a further question is presented, whether the petitioner, during the taxable year, was engaged in trade or business within the United States. If this question is decided affirmatively, it follows that the capital gain is taxable by reason of the provisions of section 211 (b) of the Internal Revenue Code.

FINDINGS OF FACT.

The facts which have been stipulated are found as facts. The written stipulations of facts together with the attached exhibits, and the oral stipulations of facts are incorporated herein by this reference.

Petitioner's income tax return for the calendar year 1946 was filed with the collector for the district of Maryland. The return was filed on the basis that petitioner was a nonresident alien of the United States not engaged in trade or business in the United States.

Petitioner's full name is Jan Casimir Eric Emil Lewenhaupt. He is a Swedish Count. He was born on April 1, 1916. From the date of his birth to November 1948 he was a nonresident alien and a resident and citizen of the Kingdom of Sweden. Petitioner became a resident of the United States in November 1948. The petitioner was physically present in the United States during the

calendar year 1946 only from November 20, 1946, to December 20, 1946. At no time prior to November 1948 did the petitioner perform any personal services within the United States. From 1941 through 1946, except for the periods during which he was in the Swedish Army, petitioner was engaged in the importing and exporting business in Sweden. During World War II, petitioner spent several periods in the Swedish Army, and for a portion of this time his regiment was located on the northern border of Sweden, an isolated location with which communication was difficult. From about 1939 through 1945, petitioner was unable to leave Sweden to come to the United States. During the Russo-Finnish War, petitioner served as a volunteer in the Finnish Army. Petitioner owned no real estate in Europe in 1946 or in any of the years prior thereto.

In 1874, petitioner's great-grandfather, Serranus Clinton Hastings, the first Chief Justice of California, created an inter vivos trust for the benefit of himself, his wife, and their descendants. This trust, sometimes hereinafter referred to as the Hastings trust, terminated on June 2, 1942, when the last of the children of Judge Hastings died. At the time that this trust terminated, Clinton LaMontagne was the trustee. From June 2, 1942, to March 31, 1945, inclusive, LaMontagne acted as referee in the partition of the corpus of the trust. The corpus was liquidated and distributed to the remaindermen in cash. The [pg. 153]last of the distributions of corpus was made on or before March 31, 1945.

Prior to the calendar year 1941, petitioner owned no real or personal property in the United States. He was, however, the beneficiary of a trust established under the will of his mother, Azelea Caroline Lewenhaupt, hereinafter sometimes referred to as the Lewenhaupt trust, the corpus of which comprised four parcels of real property and securities in the United States. Petitioner's mother died in 1925. Under the provisions of the trust established by her will, the petitioner received the income therefrom until he attained the age of 25, at which time the trust terminated and the corpus was distributed to him. Petitioner attained the age of 25 years on April 1, 1941.

On January 28, 1941, the petitioner appointed LaMontagne, who was a resident of California, as his agent for the purpose of managing the personal and real property petitioner was to receive upon distribution of the assets of the Hastings and of the Lewenhaupt trusts. LaMontagne was a second cousin of the petitioner and had been a trustee of the Hastings trust. The power of attorney dated January 28, 1941, executed by the petitioner in favor of LaMontagne conferred broad general powers on LaMontagne to manage petitioner's affairs and property in the United States, including the power to buy and sell real estate and securities, and "to do and transact all and every kind of business of what nature and kind soever" for and in the name of the petitioner. On the same date, the petitioner executed a power of attorney with identical provisions in favor of his father, Count Eric Audley Hall Lewenhaupt, who at all times material hereto was a resident of Great Britain.

Petitioner gave LaMontagne a broad power of attorney so that he might be able to act for him in case both Sweden and the United Kingdom were cut off from the United States and so that he would have sufficient power to handle petitioner's funds should the funds of Swedish nationals be frozen in the United States. The funds of Norwegian and Danish nationals in the United States were frozen on April 10, 1940. The funds of Swedish nationals in the United States were frozen on June 14, 1941. Petitioner gave his father a power of attorney because it was feared that Sweden might be invaded or cut off from contact with the United States and England, so that he could no longer communicate with his father in England or with LaMontagne in the United States.

From 1945 to the time of the trial of this proceeding, LaMontagne has been a real estate broker, licensed under the laws of California, and he has been engaged full time in the business of real estate brokerage and property management. He conducted this business from an office which he maintained at 369 Pine Street in San Francisco during [pg. 154]1946, as well as before that year; and during 1946, he maintained, also, an office at his home in Atherton, a suburb of San Francisco. Prior to 1945 the petitioner paid LaMontagne a fee for his services plus an amount to cover part of his office expense in San Francisco. In 1945 and 1946 LaMontagne received from the petitioner an increased fee for his services but no separate sum as reimbursement for office expense. His compensation for 1946 was in the amount of $7,580.

It was understood among petitioner, his father, and LaMontagne that LaMontagne was to take no important action regarding petitioner's United States property, such as purchasing and selling real estate, without first consulting either petitioner or petitioner's father. Prior to taking any major action with respect to petitioner's property in the United States, LaMontagne would consult with petitioner's father and, where practicable, with petitioner. Prior to selling petitioner's Modesto real property, referred to hereinafter, LaMontagne sought and received Count Eric Lewenhaupt's approval of the proposed sale. LaMontagne corresponded frequently with Count Eric Lewenhaupt. They corresponded about once or twice a week during the period from April 1, 1941, to December 31, 1946, inclusive. LaMontagne furnished petitioner's father with monthly reports of petitioner's United States properties. Petitioner frequently corresponded with his father regarding his properties in the United States.

The power of attorney given LaMontagne was revoked by the petitioner effective December 31, 1946.

LaMontagne, in the management of petitioner's properties, inter alia, executed leases, rented properties, collected the rents, kept books of account, paid taxes and mortgage interest, insured the properties, executed an option to purchase the El Camino Real property (referred to hereinafter), executed the sale of the Modesto property, and supervised repairs.

All of the income from petitioner's United States real property and securities, after payment of the expenses thereof, was transmitted to petitioner and his father.

The petitioner at one time or another during the calendar year 1946 held legal title to and owned only the following real property situated in the United States:

a. Lots 29, 30, 31 and 32 in Block 68, 10th and J Streets, Modesto, California, hereinafter referred to as "the Modesto property."

b. 1786-90 San Jose Avenue, San Francisco, California, hereinafter referred to as "the San Jose Ave. property."

c. 679-85 Sutter Street, San Francisco, California, hereinafter referred to as "the Sutter St. property."

d. 114 West Poplar Avenue, San Mateo, California, hereinafter referred to as "the West Poplar property."

[pg. 155]

The approximate fair market values of the United States real properties owned by petitioner in 1946 were as follows:

Modesto property	$240,000
Sutter Street property	75,000
San Jose Avenue property	22,000

The Modesto property consisted of a single structure containing several stores. This property was acquired by petitioner on April 1, 1941, upon termination of the Lewenhaupt trust created for his benefit under the will of his mother. The property was encumbered by a mortgage in the amount of $24,500. On January 12, 1938, while it comprised a part of the corpus of the Lewenhaupt trust, the Modesto property was leased to the Stelling Leasehold Corporation, a California corporation (the name of which was later changed to the Stelling Properties Corporation), for a 50-year term commencing January 1, 1938. On January 12, 1938, petitioner executed an agreement, in which, as beneficiary of the trust, he undertook to be bound by the lease. On December 20, 1945, petitioner through LaMontagne entered into an agreement with the Stelling Properties Corporation for the sale of the Modesto property to that corporation. LaMontagne communicated with petitioner's father before making the agreement and secured his approval thereof. Legal title to the Modesto property was transferred to the Stelling Properties Corporation on January 23, 1946. The long-term capital gain from the sale of the Modesto property was $152,555.87 computed as follows:

Net selling price		$238,903.40
Basis of improvements	$52,648.50	
Depreciation allowable	20,155.47	
Adjusted basis	$32,493.03	
Basis of land	53,854.50	
Total basis		86,347.53
Long-term capital gain		$152,555.87

The lease on the Modesto property was a so-called "net lease" under which the lessee paid all property taxes, all charges for utilities, all insurance; made all repairs, and took care of maintenance. Also, the lessee had the right to make alterations, additions, and improvements, and he was permitted to sublease the property. Petitioner, accordingly, did not pay taxes, insurance, utilities charges, or expenses of maintenance, repairs, or janitor services.

Petitioner through LaMontagne regularly made payments of interest upon the $24,500 mortgage on the Modesto property, but he made no payment of principal until the date of the sale of that property. Petitioner through LaMontagne paid the mortgage in full upon the date of the sale of the property.[pg. 156]

Petitioner is entitled to an additional deduction for depreciation for the calendar year 1946 in the amount of $66.35 rather than the $175.50 additional allowance made by the Commissioner's notice of deficiency.

The property at 1786-90 San Jose Avenue, San Francisco, consisted of a single structure containing three stores. Petitioner through LaMontagne acquired this property on October 24, 1941, in exchange for a parcel of real property acquired upon the termination in 1941 of the trust created under his mother's will. During 1946, all three stores were leased to various tenants under leases with terms of 3 years or more. On March 1, 1945, petitioner through LaMontagne leased the store at 1788 San Jose Avenue to a tenant on a month-to-month basis. This lease was operative from March 15, 1945, through February 28, 1946. A new lease was entered into with the same lessee on February 1, 1946, to be effective for a 3-year term commencing March 1,

1946. The lessee used this store as an electrical repair and radio shop. The store at 1786 San Jose Avenue was leased to a tenant from at least November 1941 through February 28, 1949, and was used as a beauty shop. On January 31, 1946, petitioner through LaMontagne leased this store to the same tenant to be effective for a 3-year term commencing February 1, 1946. The store at 1790 San Jose Avenue was leased to a tenant from at least November 1941 through December 1948 for use as a restaurant and tavern. The lease in effect during 1946 was for a 3-year and 4-month term. All of the leases in effect during 1946 provided that the tenants would pay all utility bills and would make certain repairs at their own expense, except repairs of heating, roof, walls, and other outside repairs.

Petitioner through LaMontagne purchased the real property at 679-85 Sutter Street, San Francisco, on December 3, 1945, at a cost of $79,645.36. This property comprised a building containing two stores and ten studios (which studios were leased as a unit). On October 10, 1945, prior to the purchase of this property by the petitioner through LaMontagne, the store at 679 Sutter Street had been leased by its then owner for a 3-year term for use as a cocktail lounge commencing October 1, 1945, and ending September 30, 1948. Under this lease, the monthly rental was $300, or 7 per cent of the gross receipts of the business, whichever was larger. The petitioner, or his agents, were authorized to examine the lessee's books of account in order to check upon the amount of rent due. On December 27, 1945, the petitioner through LaMontagne leased the store at 681 Sutter Street for a 3-year term commencing January 1, 1946, for use as a ladies tailor shop. The remaining portion of the Sutter Street property, 683-5 Sutter Street, consisted of ten studios and a basement, which were leased as a unit. On December 27, 1945, petitioner through [pg. 157]LaMontagne leased this portion of the property to a tenant for a 3-year term commencing January 1, 1946. The lessee was specifically granted the power to sublease any and all of the studios. This lease was in effect through December 31, 1949. All these leases provided that the lessees should pay all utilities charges and some expenses of repairs, except repairs of heating, roof, wall, and other outside repairs.

On December 18, 1946, petitioner became the owner of real property located at 114 West Poplar Avenue, San Mateo, California, hereinafter referred to as the "West Poplar property." The cost of this property was $29,500, and included the assumption of a mortgage in the amount of $16,211.31. The improvements thereon comprised a residence. The property was vacant from December 18, 1946, to December 31, 1946, inclusive. During the calendar year 1947, the property was leased to a tenant on a month-to-month basis.

There was no mortgage or other indebtedness upon any of the real properties owned by the petitioner during the calendar year 1946 except the mortgage indebtedness on the Modesto and West Poplar properties referred to above.

Petitioner neither paid for nor furnished any janitorial services or utilities for any of the United States real properties owned by him during any of the calendar years 1942 through 1947.

The gross rentals received by petitioner from his United States real properties during the calendar year 1946, and the expenses thereof during 1946, were as follows:

	Modesto property	San Jose Avenue property	Sutter St. property	Total
Gross rentals	$843.31	$2,093.00	$8,705.99	$11,642.30
Taxes		277.66	2,541.02	2,818.68
Insurance		106.01	472.24	578.25

Maintenance and repair		56.09	3,073.15	3,129.24
Interest	94.38			94.38
Depreciation	66.35	1,236.95	2,389.37	3,692.67
Net rentals	682.58	416.29	230.21	1,329.08

On June 12, 1946, the petitioner through LaMontagne decided to purchase real property located at 100-104 South El Camino Real, San Mateo, California. This property is hereinafter referred to as "the El Camino Real property." On that date, he took an option upon said property, made a down payment of $10,000, and paid a commission of $3,375 thereon. On January 2, 1947, petitioner through LaMontagne exercised the option and acquired legal title to this property on that date. Petitioner neither received any rent nor paid nor incurred any expenses with regard to this property prior to January 1, 1947. The cost of this property was $67,500. The improvements thereon comprised a single structure containing three stores. Prior to the acquisition of legal title to this property by petitioner, [pg. 158]all three stores had been leased to different lessees by the then owner, each of said leases being for a 5-year term expiring on June 30, 1951. Petitioner still owned this property on December 31, 1947.

During the calendar year 1946, petitioner received dividends from United States sources in the amount of $8,511.25 and received interest from United States sources in the amount of $21.34. The parties have stipulated that under the provisions of article VII of the tax convention between the United States and Sweden, United States income taxes on such dividends are limited to 10 per cent of the amount of such dividends.

During 1946, petitioner owned United States securities with an approximate valuation of $100,000. Except for cash in the bank and a small amount of cash on hand, petitioner owned no other personal property in the United States during 1946.

LaMontagne, during the taxable year, devoted approximately 50 per cent of his time to the management of the petitioner's properties and to the conduct of his affairs in the United States.

The petitioner's activities during the taxable year connected with the ownership of real property located in the United States, and the management thereof through a resident agent, constituted engaging in a business during 1946 in the United States.

OPINION.

Harron, Judge:

Issue 1. The initial question is whether a capital gain from the sale in 1946 of real property situated in the United States by a citizen and resident of Sweden, is exempt from income tax by the United States under the provisions of article IX of the tax convention for the avoidance of double taxation between the United States and Sweden. Section 22 (b) (7) of the Internal Revenue Code excludes from income, "income of any kind, to the extent required by any treaty obligation of the United States."Articles V and IX of the tax convention between the United States and Sweden, effective as of January 1, 1940, read as follows:Article V.Income of whatever nature derived from real property, including gains derived from the sale of such property, but not including interest from mortgages or bonds secured by real property, shall be taxable only in the contracting State in which the real property is situated.Article IX.Gains derived in one of the contracting States from the sale or exchange of capital assets by a resident

or a corporation or other entity of the other contracting State shall be exempt from taxation in the former State provided[pg. 159] such resident or corporation or other entity has no permanent establishment in the former State.Article XXI of the tax convention authorizes the contracting states to "prescribe regulations necessary to interpret and carry out the provisions of this convention."The Commissioner's regulations issued pursuant to the tax convention with Sweden are contained in T. D. 4975, C. B. 1940-2, p. 51. Sections 25.6 and 25.10 of the regulations which interpret the provisions of articles V and IX, respectively, of the convention are printed, in pertinent parts, in the margin. 1 Section 25.6 provides that income from real property situated in the United States "including gains derived from the sale of such property" is not exempt from taxation by the United States under the convention, and that the treatment of such income for the purpose of taxation by the United States is governed by the provisions of the Internal Revenue Code (section 211) applicable generally to the taxation of nonresident aliens. 2 Section 25.10 excludes capital gains from the sale of real property situated in the United States from the provisions of article IX of the convention.The petitioner contends that he had no "permanent establishment" in the United States during the taxable year and that the gain in question being derived from a capital asset is, therefore, exempt from tax by the United States under article IX of the convention. He argues that the Commissioner's regulations are invalid in so far as they exclude capital gains from the sale of real property situated in the United States from the provisions of article IX of the convention. The petitioner takes the position that article V of the convention merely prohibits Sweden from taxing the gain in question and that "the intent of the Tax Convention was to exempt capital gains from the sale of real property from both Swedish and United States income taxes except where the seller had a permanent establishment in the United States." The respondent contends that the provisions of the regulations are in accord with the intent and purpose of the convention and are a reasonable interpretation of its provisions, and hence are valid. We agree with the respondent.[pg. 160]A tax convention or treaty is construed by the courts in the same manner as is a taxing statute. Where there is an inconsistency or conflict in the text of either, a clarifying regulation is not only appropriate but is to be given great weight by the courts. Koshland v.Helvering , 298 U. S. 441, 446. And the regulation, if in harmony with the intent and purpose of the statute or tax convention and a reasonable interpretation of its provisions, is to be sustained.In the instant case, there is a seeming inconsistency or conflict between the provisions of articles V and IX of the tax convention with respect to the treatment to be accorded a capital gain from the sale of real property, which is admittedly a capital asset. We are satisfied, from a review of the commentary on the draft of the tax convention, that the challenged provisions of the regulations are in accord with the intent and purpose of the convention, and are consistent with its provisions. See, Senate Executive Report No. 18, 76th Cong., 1st Sess. (1939).The purpose of the tax convention is the avoidance of double taxation. It was not designed, as the petitioner urges here, to exempt a class of income from taxation by both of the contracting states. "The articles of the convention dealing with avoidance of double taxation cover the whole field of taxable income, each specific item of income being made subject to tax in one or the other of the two countries but not in both." Senate Executive Reportsupra , p. 17. Although not necessary to our decision, reference should be made to the fact that Sweden, unlike the United States, does not use citizenship as a basis for taxation. Article XIV of the convention 3 was made the key provision by means of which most of the articles dealing with the [pg. 161]avoidance of double taxation with respect to specific items of income were rendered possible. Senate Executive Report, supra, p. 11.The Senate Executive Report, supra, in commenting on article IX of the draft, which covers gains from the sale or exchange of capital assets, makes no reference to gains from the sale or exchange of real property; the only class of property mentioned is securities. 4 The inference is reasonable and we think proper that the contracting states, having specifically provided in article V for the treatment

for tax purposes of income and gain from the sale of real property, with the situs of the real property made the basis for taxation, did not intend that capital gains from the sale of real property should fall within the provisions of article IX, which ties the taxation of capital gains to a permanent establishment.In any event, a review of the commentary on the proposed draft of the convention convinces us that no substantial change in the treatment for tax purposes by the United States of capital gains, whether derived from the sale of real property or from the sale of other capital assets situated in the United States by a citizen and resident of Sweden, was intended under the provisions of the convention. In this respect the provisions of articles V and IX of the convention dovetailed into our existing laws. Senate Executive Report, supra, pp. 7, 8. Under our laws in effect when the convention was ratified, the taxability by the United States of capital gains derived by a nonresident alien from sources within the United States depended on whether the nonresident alien had a "United States business or office," i. e., was engaged in trade or business within the United States. See section 211 of the Internal Revenue Code as it read prior to amendments made by the Revenue Act of 1950. The meaning of the term "permanent establishment" as used in the convention is substantially identical with the meaning of the words "United States business or office" as used in section 211 (b) of the Code. Senate Executive Report, supra, p. 7. Hence the same test for determining the taxability by the United States of a capital gain derived from the sale by a citizen and resident of Sweden of real property situated in the United States is applicable even if the provisions of article IX of the convention were construed as embracing gains from the sale of real property. Viewed in this light, the seeming conflict in the text of the convention between the provisions of articles V and IX is dispelled.[pg. 162]We conclude that the Commissioner's regulations issued pursuant to the tax convention with Sweden, in so far as they reflect the treatment for tax purposes by the United States of gains derived from the sale of real property situated in the United States, are valid. We therefore hold that the gain derived from the sale in 1946 of real property situated in the United States by the petitioner is not exempt from income tax by the United States under the provisions of article IX of the tax convention with Sweden.

Issue 2. The remaining issue is whether the petitioner, during the taxable year, was engaged in trade or business in the United States within the meaning of section 211(b) of the Internal Revenue Code. If the petitioner was so engaged the capital gain in question is taxable under the provisions of section 117 of the Internal Revenue Code. Section 211(b) of the Code, which is printed in the margin, 5 provides that nonresident aliens who are engaged in a trade or business in the United States are taxable in the same manner as citizens of the United States with respect to income derived from sources within the United States.

The issue here is whether the petitioner's activities with respect to certain parcels of improved real estate constituted engaging in a trade or business. The petitioner, during the taxable year, did not trade in, or realize gain from the sale or exchange of, securities or commodities. At the beginning of the taxable year, the petitioner owned United States securities of an approximate value of $100,000. His only security transactions during the taxable year were the purchase of additional securities with part of the proceeds from the sale of the Modesto real property, which gave rise to the capital gain in question. The respondent's argument on brief that petitioner failed to show that his security transactions did not constitute engaging in business is without merit. See Higgins v.Commissioner , 312 U. S. 212; Evelyn M. L. Neill, 46 B. T. A. 197.

Whether the activities of a nonresident alien constitute engaging in a trade or business in the United States, is, in each instance, a question of fact. The evidence and record before us establish, and we have found as a fact, that the petitioner's activities during the taxable [pg. 163]year connected with his ownership, and the management through a resident agent, of real

property situated in the United States constituted engaging in a business. The petitioner, prior to and during the taxable year, employed LaMontagne as his resident agent who, under a broad power of attorney which included the power to buy, sell, lease, and mortgage real estate for and in the name of the petitioner, managed the petitioner's real properties and other financial affairs in this country. The petitioner, during all or a part of the taxable year, owned three parcels of improved, commercial real estate. The approximate aggregate fair market value of the three properties was $337,000. In addition, the petitioner purchased a residential property, and through his agent, LaMontagne, acquired an option to purchase a fourth parcel of commercial property, herein referred to as the El Camino Real property, at a cost of $67,500. The option was exercised and title to the property conveyed to the petitioner in January 1947.

LaMontagne's activities, during the taxable year, in the management and operation of petitioner's real properties included the following: executing leases and renting the properties, collecting the rents, keeping books of account, supervising any necessary repairs to the properties, paying taxes and mortgage interest, insuring the properties, executing an option to purchase the El Camino Real property, and executing the sale of the Modesto property. In addition, the agent conducted a regular correspondence with the petitioner's father in England who held a power of attorney from petitioner identical with that given to LaMontagne; he submitted monthly reports to the petitioner's father; and he advised him of prospective and advantageous sales or purchases of property.

The aforementioned activities, carried on in the petitioner's behalf by his agent, are beyond the scope of mere ownership of real property, or the receipt of income from real property. The activities were considerable, continuous, and regular and, in our opinion, constituted engaging in a business within the meaning of section 211 (b) of the Code. SeePinchot v. Commissioner, 113 F. 2d 718.

Evelyn M. L. Neill, supra, and other authorities relied on by the petitioner, are distinguishable on the facts from this proceeding. The decisions of state courts cited by the petitioner defining what constitutes engaging in a trade or business under various state laws are not persuasive here. Pinchot v. Commissioner, supra.

We hold that the petitioner, during the taxable year, was engaged in a trade or business, and that his income from sources within the United States is taxable under section 211 (b) of the Code.

Reviewed by the Court.

Decision will be entered under Rule 50.

1 Sec. 25.6. Income from real property.-Income of whatever nature derived by a nonresident alien individual resident in Sweden

*** from real property situated in the United States, including gains derived from the sale of such property, is not exempt from taxation by the convention. The treatment of such income for taxation purposes is governed by those provisions of the Internal Revenue Code applicable generally to the taxation of nonresident aliens

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Sec. 25.10. Capital gains.-Under Article IX of the convention gain derived from the sale or exchange of capital assets (other than real property) within the United States by a nonresident alien individual resident in Sweden

*** is exempt from Federal income tax unless such individual

*** has a permanent establishment in the United States. With respect to real property, see sec. 25.6 of these regulations.

2 Prior to 1950 nonresident aliens not engaged in trade or business in the United States were taxed only on the amount of fixed or determinable annual or periodic income from sources within the United States. They were not taxed on any capital gains unless engaged in business in the United States. See sec. 211 of the Internal Revenue Code and Regs. 111, sec. 29.143-2.

3 Article XIV reads as follows:

It is agreed that double taxation shall be avoided in the following manner:

(a) Notwithstanding any other provisions of this convention, the United States of America in determining the income and excess-profits taxes, including all surtaxes, of its citizens or residents or corporations, may include in the basis upon which such taxes are imposed all items of income taxable under the revenue laws of the United States of America as though this convention had not come into effect. The United States of America shall, however, deduct the amount of the taxes specified in Article I (b) (1) and (3) of this convention or other like taxes from the income tax thus computed but not in excess of that portion of the income tax liability which the taxpayer's net income taxable in Sweden bears to his entire net income.

(b) (1) Notwithstanding any other provision of this convention, Sweden, in determining the graduated tax on income and property of its residents or corporations or other entities, may include in the basis upon which such tax is imposed all items of income and property subject to such tax under the taxation laws of Sweden. Sweden shall, however, deduct from the tax so calculated that portion of such tax liability which the taxpayer's income and property exempt from taxation in Sweden under the provisions of this convention bears to his entire income and property.

(2) There shall also be allowed by Sweden from its national income and property tax a deduction offsetting the tax deducted at the source in the United States of America, amounting to not less than 5 per centum of the dividends from within the United States of America and subject to such tax in Sweden. It is agreed that the United States of America shall allow a similar credit against the United States income tax liability of citizens of Sweden residing in the United States of America.

4 Senate Executive Report No. 18,supra, p. 8:

Article IX, as already noticed, ties the taxation of capital gains to a permanent establishment. If, for example, a Swedish corporation has no permanent establishment in the United States and sells securities on the New York Stock Exchange, the resultant gains, if any, are not taxable under

*** this article. This principle is in accord with our existing law under which a corporation falling within the provisions of section 231 (a) or a nonresident alien falling within the provisions of section 211 (a), is not subject to tax on the gain derived from the sale or exchange of securities through a resident broker, commission agent, or custodian.

5 SEC. 211. TAX ON NONRESIDENT ALIEN INDIVIDUALS.

*** (b) United States Business or Office.-A nonresident alien individual engaged in trade or business in the United States shall be taxable without regard to the provisions of subsection (a). As used in this section, section 119, section 143, section 144, and section 231, the phrase "engaged in trade or business within the United States" includes the performance of personal services within the United States at any time within the taxable year, but does not include the performance of personal services for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of ninety days during the taxable year and whose compensation for such services does not exceed in the aggregate $3,000. Such phrase does not include the effecting, through a resident broker, commission agent, or custodian, of transactions in the United States in commodities

*** or in stocks or securities.