10 T.C. 77 (1948)

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Interest paid by a U.S. corporation to a nonresident alien is considered income from sources within the United States, requiring the corporation to withhold income tax, even if the payment is made from a foreign branch’s bank account.

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Summary

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A. C. Monk & Company, a U.S. corporation, operated a branch in China and paid interest to a Chinese national, Tsze E. Pun, on deposits he made as part of his sales agency agreement. These payments were made from the branch’s Chinese bank accounts. The Tax Court held that this interest constituted income to the Chinese national from sources within the United States, requiring A. C. Monk to withhold income tax. The court rejected the argument that the source of the income was China because the payments were made there, emphasizing that the obligation to pay interest arose from the U.S. corporation.

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Facts

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A. C. Monk & Company, a North Carolina corporation, sold tobacco in China. Tsze E. Pun, a Chinese national, acted as their sales agent. In 1931, they entered into a written agreement where Pun became the sole agent and sales manager for Asia. Pun was required to deposit $15,000 with the company, and the company would pay him 6% interest on the deposit. The deposits protected the company on sales made on credit. Pun’s deposits varied between $10,000 and $40,500. The interest payments were made from the company’s bank accounts in China and charged to the expenses of the Chinese branch. The IRS assessed deficiencies for failure to withhold taxes on these interest payments.

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Procedural History

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The Commissioner of Internal Revenue determined deficiencies against A. C. Monk & Company for failure to withhold income tax on interest payments made to a nonresident alien. A. C. Monk & Company petitioned the Tax Court for a redetermination of these deficiencies.

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Issue(s)

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Whether interest paid by a U.S. corporation to a nonresident alien, from a bank account maintained in China for its Chinese branch, constitutes income from sources within the United States and is subject to withholding tax.

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Holding

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Yes, because the interest payments were an interest-bearing obligation of a U.S. resident corporation, making it income from a U.S. source under the applicable statute, regardless of where the payments were physically made.

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Court’s Reasoning

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The Tax Court relied on Section 119 of the Internal Revenue Code, which defines gross income from sources within the United States to include interest from a U.S. resident’s interest-bearing obligations. The court found that the payments to Pun were indeed interest on an interest-bearing obligation, rejecting the argument that

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