*1954 Tax Ct. Memo LEXIS 109*

An entity created by a foreign government to promote national production and improve the standard of living, closely coordinated with the government, supported by taxes, and with international borrowings on the nation's credit, is considered part of that foreign government for purposes of U.S. tax exemptions for its employees.

**Summary**

The petitioners, citizens of Chile, were employed in the U.S. by Corporación de Fomento de la Producción (Fomento) and sought exemption from U.S. income tax under Section 116(h) of the Internal Revenue Code, which exempts compensation paid to employees of foreign governments under certain conditions. The Tax Court addressed whether Fomento was part of the Chilean government or a separate instrumentality. The court held that Fomento was an integral part of the Chilean government, and thus its employees were entitled to the tax exemption.

**Facts**

Fomento was created by Chilean law as a "legal person" charged with promoting national production to raise the standard of living. It lacked shareholders and was administered by a council composed of government officials and representatives from various sectors of Chilean society. Fomento's responsibilities included creating a general plan for the promotion of national production, conducting studies, aiding manufacturing, and securing financing. It was funded by taxes, loans (including from the Export-Import Bank), and income from its projects. The petitioners, all engineers, were sent to the U.S. to gain technical knowledge and supervise the acquisition of equipment for projects in Chile.

**Procedural History**

The Commissioner of Internal Revenue determined deficiencies in the petitioners' income tax for the years 1946 and 1947. The petitioners challenged this determination, arguing they were exempt from U.S. income tax under Section 116(h) of the Internal Revenue Code as employees of a foreign government. The Tax Court reviewed the case based on a stipulated set of facts.

**Issue(s)**

Whether Corporación de Fomento de la Producción was a part of the Government of Chile for the purpose of Section 116(h) of the Internal Revenue Code, thus entitling its employees to exemption from U.S. income tax.

**Holding**

Yes, because Fomento was created by public law, closely coordinated with the Chilean government, supported by taxes and national credit, and its employees were

© 2025 SCOTUSreports.com. All rights reserved. 

considered government employees by both the Chilean government and the U.S. Department of State.

### Court’s Reasoning

The court reasoned that Fomento was not a corporation in the U.S. sense. It emphasized Fomento’s public function and governmental powers, contrasting it with private corporations (“Sociedad Anónima”). Fomento’s governing body was fixed by law, its operations were regulated and supervised by government entities, and its goals were national in scope. The court considered Fomento a part of the Chilean government, similar to a national resources planning board. The court noted that Fomento was created by public law, headed by a cabinet member, and largely supported by taxes. The court also emphasized the Secretary of State’s certification that U.S. government employees in Chile received equivalent tax exemptions and performed similar services. The court referenced the purpose of Section 116(h), which was to obtain reciprocity for U.S. government employees abroad. The court stated, “The Court, in reaching its conclusion that these petitioners are exempt, has considered not only that part of the stipulation referred to or discussed herein, but every portion of that stipulation, including some portions not favorable to the contention, of the petitioners. The conclusion was reached because there was a preponderance of evidence in favor of it.”

### Practical Implications

This case clarifies the criteria for determining whether an entity is part of a foreign government for the purpose of U.S. tax exemptions. It highlights the importance of examining the entity’s creation, governance, funding, and relationship with the foreign government. The ruling emphasizes that the laws of different countries vary, and an exact counterpart to a foreign entity is not required for it to be considered part of the government. The State Department’s view carries significant weight in determining whether reciprocity exists. Later cases would likely analyze these same factors to determine if a similar organization’s employees qualify for the tax exemption. It informs how U.S. tax authorities evaluate claims of foreign government employee status, particularly regarding entities with quasi-governmental functions. It is fact-specific and highlights the importance of a comprehensive stipulation of facts to demonstrate the nature of the foreign entity and its relationship to the foreign government.

© 2025 SCOTUSreports.com. All rights reserved. 