

“(1) gross income which is derived from sources within the United States and which is not effectively connected with the conduct of a trade or business within the United States, and

“(2) gross income which is effectively connected with the conduct of a trade or business within the United States.”

(2) Subparagraph (B) of section 872(b) (3) relating to compensation of participants in certain exchange or training programs) is amended by striking out “by a domestic corporation” and inserting in lieu thereof “by a domestic corporation, a domestic partnership, or an individual who is a citizen or resident of the United States”.

(3) Subsection (b) of section 872 (relating to exclusions from gross income) is amended by adding at the end thereof the following new paragraph:

“(4) **BOND INTEREST OF RESIDENTS OF THE RYUKYU ISLANDS OR THE TRUST TERRITORY OF THE PACIFIC ISLANDS.**—Income derived by a nonresident alien individual from a series E or series H United States savings bond, if such individual acquired such bond while a resident of the Ryukyu Islands or the Trust Territory of the Pacific Islands.”

(c) **DEDUCTIONS.**—

(1) Section 873 (relating to deductions allowed to nonresident alien individuals) is amended to read as follows:

“SEC. 873. DEDUCTIONS.

“(a) **GENERAL RULE.**—In the case of a nonresident alien individual, the deductions shall be allowed only for purposes of section 871(b) and (except as provided by subsection (b)) only if and to the extent that they are effectively connected with the conduct of a trade or business within the United States; and the proper apportionment and allocation of the deductions for this purpose shall be determined as provided in regulations prescribed by the Secretary or his delegate.

“(b) **EXCEPTIONS.**—The following deductions shall be allowed whether or not they are effectively connected with the conduct of a trade or business within the United States:

“(1) **LOSSES.**—The deduction, for losses of property not connected with the trade or business if arising from certain casualties or theft, allowed by section 165(c) (3), but only if the loss is of property located within the United States.

“(2) **CHARITABLE CONTRIBUTIONS.**—The deduction for charitable contributions and gifts allowed by section 170.

“(3) **PERSONAL EXEMPTIONS.**—The deduction for personal exemptions allowed by section 151, except that in the case of a nonresident alien individual who is not a resident of a contiguous country only one exemption shall be allowed under section 151.

“(c) **CROSS REFERENCES.**—

“(1) For disallowance of standard deduction, see section 142(b)(1).

“(2) For rule that certain foreign taxes are not to be taken into account in determining deduction or credit, see section 906(b)(1).”

(2) Section 154(3) (relating to cross references in respect of deductions for personal exemptions) is amended to read as follows: