problems your committee's bill repeals this special foreign-source rule but also postpones the effective date of the repeal until after 1971. At that time your committee will have an opportunity to reconsider the balance-of-payments situation.

It also is the opinion of your committee that, as long as bank deposit interest is to be treated as foreign source income, there is no justification for denying similar treatment for interest paid by savings and loan institutions generally as well as interest earned on the proceeds of an insurance policy which are left on deposit with an insurance company. These all represent interest income received on deposits and, therefore, it is believed that the competing businesses should be treated in the same manner for tax purposes.

(*c*) *Explanation of provision.*—For the above reasons your committee has amended present law to provide that after December 31, 1971, interest on deposits with U.S. banks paid to nonresident alien individuals or foreign corporations is to be treated as income from sources within the United States. Therefore, until 1972 only interest which is effectively connected with the conduct of a trade or business in the United States will be subject to U.S. tax.[1] In addition, during the intervening 5-year period your committee has extended the application of the foreign source rule of present law to interest (or so-called dividends) paid on deposits (or withdrawable accounts) with all chartered and supervised savings and loan associations or similar institutions, to the extent these amounts are deductible in computing the taxable income of these institutions. Similar institutions for this purpose include mutual savings banks, cooperative banks, and domestic building and loan associations. Also, during this 5-year period, this special foreign source rule is to be applicable to interest on amounts held by insurance companies under an agreement to pay interest. The amounts paid by insurance companies to which this rule is extended include: (1) interest paid on policyholder dividends left with the company to accumulate; (2) interest paid on prepaid insurance premiums; (3) interest paid on proceeds of policies left on deposit; and (4) interest paid on overcharges of premiums.

(*d*) *Effective date.*—Except for the provision repealing the special foreign source rule for certain interest as of December 31, 1971, these amendments are effective with respect to taxable years beginning after December 31, 1966.

2. Interest on deposits in foreign branch banks of domestic corporations (sec. 2(a)(2) of the bill, sec. 861(a)(1)(D) of the code)

(*a*) *Present law.*—Present law provides that interest paid to nonresident alien individuals or foreign corporations on deposits with foreign branch banks of U.S. corporations, although paid by the foreign branch situated abroad, is treated as from sources within the United States if the recipient of the interest is engaged in a trade or business in the United States. This is true whether the deposits are payable in dollars or in the currency of the foreign country where the branch is located.

(*b*) *Reasons for provision.*—As a result of the rule described above nonresident aliens and foreign corporations often are reluctant to

[1] The term "effectively connected" is explained subsequently in No. B–2 below under sec. 2(d) of the bill.