SECTION 2 OF BILL. SOURCE OF INCOME

(*a*) *Interest.*—Subsection (a) of section 2 of the bill amends section 861 of the code (relating to income from sources within the United States) in its application to interest income and section 895 of the code (relating to income derived by a foreign central bank of issue from obligations of the United States).

Certain interest not treated as income from sources within the United States

Existing section 861(a)(1) provides generally that interest paid by a resident of the United States, corporate or otherwise, is income from sources within the United States. Subparagraph (A) of section 861(a)(1) excepts interest paid on deposits with persons carrying on the banking business from this rule if such interest is paid to persons not engaged in business in the United States.

Paragraph (1)(A) of section 2(a) of the bill revises existing subparagraph (A) of section 861(a)(1) to provide in effect that interest on the amounts described in new subsection (c) of section 861, as added by paragraph (1)(B) of section 2(a) of the bill, is not considered income from sources within the United States if such interest is paid (or credited) to a nonresident alien individual or foreign corporation before January 1, 1972, and such interest is not effectively connected with the conduct of a trade or business within the United States by such recipient. The amendment of section 861(a)(1)(A) is effective for taxable years beginning after December 31, 1966, but such section shall cease to apply in the case of amounts paid or credited after December 31, 1971.

Paragraph (1)(B) of section 2(a) of the bill amends section 861 of the code by adding a new subsection (c) which describes the amounts the interest on which is subject to the source rule of new section 861(a)(1)(A). The amounts so described are (1) deposits with persons carrying on the banking business (including certificates of deposit); (2) deposits or withdrawable accounts with mutual savings banks, cooperative banks, domestic building and loan associations, and other savings institutions chartered and supervised as savings and loan or similar associations under Federal or State law, but only to the extent that the amounts paid or credited on such deposits or accounts (in respect of which a determination is being made under sec. 861(a)(1)) are of a type which are deductible under section 591 of the code (relating to deductions for dividends paid on deposits) in computing the taxable income of such institutions; and (3) amounts held by an insurance company under an agreement to pay interest thereon. New section 861(c) is effective for taxable years beginning after December 31, 1966.

The rule in existing section 861(a)(1)(A) with respect to interest on bank deposits has been revised in amended section 861(a)(1)(A) so as to apply only if the interest is not effectively connected with the conduct of a trade or business within the United States and only when received by a nonresident alien individual or a foreign corporation.

Deposits and withdrawable accounts with savings and loan or similar associations are included in new section 861(c)(2) so that interest (and so-called dividends) paid on such deposits or withdrawable