

from obligations of the United States) and makes conforming amendments. Under present section 895 income derived by a foreign central bank of issue from obligations of the United States owned by such bank is excluded from gross income, if such obligations are not held for, or used in connection with, the conduct of commercial banking functions or other commercial activities of such bank. Amended section 895 continues existing law and provides a similar exclusion with respect to interest derived by a foreign central bank of issue from deposits with persons carrying on the banking business; it also contains a new provision under which the Bank for International Settlements will be entitled to exclude from gross income interest derived on deposits with persons carrying on the banking business if such deposits are not held for, or used in connection with, the conduct of commercial banking functions or other commercial activities by such depositor. These amendments are effective for taxable years beginning after December 31, 1966. It is to be noted, however, that the exclusion under section 895 for interest on deposits with persons carrying on the banking business will continue to apply in the case of amounts paid or credited after December 31, 1971, even though the provisions of amended section 861(a)(1)(A) cease to apply to amounts paid or credited after that date.

(b) *Dividends*.—Subsection (b) of section 2 of the bill amends section 861(a)(2) of the code (relating to dividends from sources within the United States).

*Dividends from foreign corporations*

Paragraph (1) of section 2(b) of the bill amends subparagraph (B) of section 861(a)(2) of the code (relating to the source of dividends from a foreign corporation). Under present section 861(a)(2)(B), if a foreign corporation derives 50 percent or more of its gross income from sources within the United States for the applicable period preceding the declaration of dividends, an amount which bears the same ratio to such dividends as the gross income of the corporation for such period from sources within the United States bears to its gross income from all sources for such period is considered to be a dividend from sources within the United States.

Under amended section 861(a)(2)(B) dividends paid by a foreign corporation are from sources within the United States only if 80 percent or more of the total gross income of such corporation from all sources for the applicable period preceding the declaration of the dividends was effectively connected with the conduct of a trade or business within the United States by such foreign corporation. The amount of the dividends treated as income from sources within the United States in such case is the amount which bears the same ratio to the dividends which are paid as the gross income of the foreign corporation for such period which is effectively connected with the conduct of a trade or business in the United States bears to the gross income of such corporation from all sources for such period. This amendment is effective with respect to dividends received after December 31, 1966; but, to the extent that gross income of the foreign corporation for any period before its first taxable year beginning after December 31, 1966, must be taken into account in determining the application of amended section 861(a)(2)(B), the gross income of such