

interest (or for such part of such period as the corporation has been in existence) was effectively connected with the conduct of a trade or business within the United States,

"(D) in the case of interest received from a foreign corporation (other than interest paid or credited after December 31, 1971, by a domestic branch of a foreign corporation, if such branch is engaged in the commercial banking business) 50 percent or more of the gross income of which from all sources for the 3-year period ending with the close of its taxable year preceding the payment of such interest (or for such part of such period as the corporation has been in existence) was effectively connected with the conduct of a trade or business within the United States, an amount of such interest which bears the same ratio to such interest as the gross income of such foreign corporation for such period which was not effectively connected with the conduct of a trade or business within the United States bears to its gross income from all sources,

"(E) income derived by a foreign central bank, of issue from bankers' acceptances, and

"(F) interest on deposits with a foreign branch of a domestic corporation or a domestic partnership, if such branch is engaged in the commercial banking business."

(3) Section 861 (relating to income from sources within the United States) is amended by adding after subsection (c) (as added by paragraph (1)(B)) the following new subsection:

"(d) SPECIAL RULES FOR APPLICATION OF PARAGRAPHS (1)(B), (1)(C), (1)(D), AND (2)(B) OF SUBSECTION (a).—

"(1) NEW ENTRIES.—For purposes of paragraphs (1)(B), (1)(C), (1)(D), and (2)(B) of subsection (a), if the resident alien individual, domestic corporation, or foreign corporation, as the case may be, has no gross income from any source for the 3-year period (or part thereof) specified, the 20 percent test or the 50 percent test, as the case may be, shall be applied with respect to the taxable year of the payor in which payment of the interest or dividends, as the case may be, is made.

"(2) TRANSITION RULE.—For purposes of paragraphs (1)(C), (1)(D), and (2)(B) of subsection (a), the gross income of the foreign corporation for any period before the first taxable year beginning after December 31, 1966, which is effectively connected with the conduct of a trade or business within the United States is an amount equal to the gross income for such period from sources within the United States."

(4)(A) Section 895 (relating to income derived by a foreign central bank of issue from obligations of the United States) is amended to read as follows:

"SEC. 895. INCOME DERIVED BY A FOREIGN CENTRAL BANK OF ISSUE FROM OBLIGATIONS OF THE UNITED STATES OR FROM BANK DEPOSITS.

"Income derived by a foreign central bank of issue from obligations of the United States or of any agency or instrumentality thereof (including beneficial interests, participations, and other instruments issued under section 302(c) of the Federal National Mortgage Association Charter Act (12 U.S.C. 1717)) which are owned by such foreign central bank of issue, or derived from interest on deposits with persons carrying on the banking business, shall not be included in gross income and shall be exempt from taxation under this subtitle unless such obliga-

tions or deposits are held for, or used in connection with, the conduct of commercial banking functions or other commercial activities. For purposes of the preceding sentence the Bank for International Settlements shall be treated as a foreign central bank of issue."

(B) The table of sections for subpart C of part II of subchapter N of chapter 1 is amended by striking out the item relating to section 895 and inserting in lieu thereof the following:

"Sec. 895. Income derived by a foreign central bank of issue from obligations of the United States or from bank deposits."

(b) DIVIDENDS.—Section 861(a)(2)(B) (relating to dividends from sources within the United States) is amended to read as follows:

"(B) from a foreign corporation unless less than 50 percent of the gross income from all sources of such foreign corporation for the 3-year period ending with the close of its taxable year preceding the declaration of such dividends (or for such part of such period as the corporation has been in existence) was effectively connected with the conduct of a trade or business within the United States; but only in an amount which bears the same ratio to such dividends as the gross income of the corporation for such period which was effectively connected with the conduct of a trade or business within the United States bears to its gross income from all sources; but dividends (other than dividends for which a deduction is allowable under section 245(b)) from a foreign corporation shall, for purposes of subpart A of part III (relating to foreign tax credit), be treated as income from sources without the United States to the extent (and only to the extent) exceeding the amount which is 100/85ths of the amount of the deduction allowable under section 245 in respect of such dividends, or".

(c) PERSONAL SERVICES.—Section 861(a)(3)(C)(ii) (relating to income from personal services) is amended to read as follows:

"(ii) an individual who is a citizen or resident of the United States, a domestic partnership, or a domestic corporation, if such labor or services are performed for an office or place of business maintained in a foreign country or in a possession of the United States by such individual, partnership, or corporation."

(d) DEFINITIONS.—Section 864 (relating to definitions) is amended—

(1) by striking out "For purposes of this part," and inserting in lieu thereof

"(a) SALE, ETC.—For purposes of this part,"; and

(2) by adding at the end thereof the following new subsections:

"(b) TRADE OR BUSINESS WITHIN THE UNITED STATES.—For purposes of this part, part II, and chapter 3, the term 'trade or business within the United States' includes the performance of personal services within the United States at any time within the taxable year, but does not include—

"(1) PERFORMANCE OF PERSONAL SERVICES FOR FOREIGN EMPLOYER.—The performance of personal services—

"(A) for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, or

"(B) for an office or place of business maintained in a foreign country or in a possession