

*banks of domestic corporations.*—Interest on deposits with foreign branch banks of U.S. corporations or partnerships is to be treated as foreign source income, and thus free of U.S. income tax when paid to nonresident aliens and foreign corporations.

*2. Source rules for bank deposit interest and similar income.*—After December 31, 1971, all interest on U.S. bank deposits (other than those described in No. 1 above), whether or not effectively connected with a U.S. business, is to be treated as U.S. source income (and subject to U.S. income tax) in the case of nonresident aliens and foreign corporations. Until then, this interest on bank deposits, interest paid on accounts with mutual savings banks, domestic building and loan associations, etc., and interest on amounts held by insurance companies on deposit also are to be treated as foreign source income (unless effectively connected with a U.S. business) and thereby free of U.S. income tax.

*3. Rules for determining the source of dividends from foreign corporations.*—The source rule with respect to dividends paid by foreign corporations is amended to provide that dividends received from a foreign corporation are to be considered as having a U.S. source only if 50 percent (House bill provided an 80-percent rule) of the corporation's gross income for the prior 3 years was effectively connected with the conduct of a trade or business in the United States.

*4. Compensation for personal services.*—The special source rule, providing that certain payments of compensation for services performed in the United States by a nonresident alien are treated as foreign source income (and therefore free of U.S. tax) if the services are performed for certain foreign persons or a foreign office of a U.S. corporation, is extended to services performed for a foreign office of a proprietor who is a citizen or resident of the United States or for the foreign office of a domestic partnership.

*5. Trading in stocks or securities or in commodities.*—Except in the case of dealers and certain investment companies, trading in stocks or securities in the United States for one's own account, whether by a foreign investor physically present in the United States, through an employee located here, or through a resident agent (whether or not the agent has discretionary authority) is not to constitute a trade or business in the United States for income tax purposes. A parallel rule is provided for those trading in commodities.

*6. Income effectively connected with the conduct of a trade or business in the United States.*—The benchmark to be used in determining whether income is to be subject to a flat 30-percent rate or taxed substantially the same as income earned here by a U.S. citizen or domestic corporation is whether or not the income is effectively connected with a U.S. business. In the case of investment and other fixed or determinable income and capital gains from U.S. sources the income is to be treated as effectively connected with a U.S. business if the income is derived from the assets used or held for use in the conduct of a U.S. business or if the activities of the U.S. business are a material factor in the realization of the income. All other types of U.S. source income are to be considered to be effectively connected if there is a U.S. business. Income from sources without the United States will not be treated as effectively connected with a U.S. business

unless the nonresident alien or foreign corporation has a fixed place of business in the United States and the income is attributable to that place of business. Moreover, in general only rents and royalties from licensing, certain income from banking and so forth, and sales income are to be taken into account for this purpose and only to the extent the income is not "subpart F" income or income derived from a foreign corporation 50 percent owned by the nonresident alien or foreign corporation receiving the income. Your committee modified the provision of the House bill dealing with "effectively connected" foreign source income to exclude (a) income derived from a transaction in which the U.S. office was not a material factor, (b) income not derived from the usual business activities of the U.S. office, and (c) income not properly allocable to the U.S. office. Additionally, the definition of a U.S. office was redefined to exclude the office of certain agents. In another modification, the foreign tax credit provision was expanded to include domiciliary taxes attributable to the foreign source income effectively connected income.

*7. Income tax on nonresident alien individuals.*—The income of nonresident aliens which is effectively connected with a U.S. business is to be taxed at the regular graduated rates applicable to individuals and all income not so connected is to be taxed at a flat 30-percent rate (or lower applicable treaty rate). U.S. source capital gains of a nonresident alien not engaged in business in the United States are to be taxed only if the alien was in the United States for 183 days or more during the year. Deductions are allowable only to the extent allocable to income which is effectively connected to a U.S. business. Also, an election is provided which allows an alien to treat income from real property as U.S. business income in order to take deductions allocable to it.

*8. Expatriation to avoid income tax.*—U.S. source income and the effectively connected income of a citizen received for 10 years after expatriation is, in most cases, to be taxed at the regular U.S. tax rates if a principal purpose of the expatriation was the avoidance of U.S. income, estate, or gift taxes. The House bill would have provided a 5-year rule for income taxes.

*9. Withheld taxes and declarations of estimated income tax.*—The Treasury Department is authorized to require payment of amounts withheld from nonresident aliens and foreign corporations on a more current basis, rather than the annual basis presently provided. Nonresident aliens who receive income which is effectively connected with the conduct of a U.S. business are to be required to file declarations of estimated tax.

*10. Income tax on foreign corporations.*—The regular corporate income tax is to apply to income of foreign corporations which is effectively connected with a U.S. business. U.S. source income which is not so connected is taxable at a flat 30-percent rate (or at a lower treaty rate). Foreign corporations are given an election to treat real property income as business income similar to that afforded nonresident aliens.

*11. Foreign corporations carrying on insurance business in the United States.*—A foreign corporation carrying on a life insurance business within the United States is to be taxed under the present special insurance company provisions on its income effectively connected with a U.S. business. The remainder of the income of this type of corporation from sources within the United