

or the District of Columbia are to be treated as income from sources within the United States regardless of where the sale or exchange occurs or title is transferred. Deductions are to be allowed only to the extent they are properly allocable to the gross income of the expatriate, determined under the above described provisions (except that the capital loss carryover provision is not to apply).

The new section contains a special rule with respect to the burden of proving the existence or nonexistence of U.S. tax avoidance as one of the principal purposes of the expatriation. Under this provision, the Secretary of the Treasury or his delegate must first establish that it is reasonable to believe that the expatriate's loss of U.S. citizenship would (but for the application of these special provisions) result in a substantial reduction in his taxes based on the expatriate's probable income for the taxable year.

If this is established, then the expatriate must carry the burden of proving that the loss of citizenship did not have, for one of its principal purposes, the avoidance of U.S. income, estate, or gift taxes. However, the new section excepts persons whose loss of citizenship occurs under circumstances where it is unlikely that tax avoidance was a principal purpose. For example, this provision does not apply where the person acquired dual citizenship at birth and loses his U.S. citizenship by residing, for a certain period, in the foreign country of which he is also a citizen by birth.

Effective date.—This amendment applies for taxable years beginning after December 31, 1966.

d. Partial exclusion of dividends from gross income (sec. 103(g) of the act and sec. 116(d) of the code)

Prior law allowed a nonresident alien the \$100 dividends received exclusion only if the individual was taxable on U.S. source dividends at the regular graduated rates applicable to individuals. The act amends this provision, effective for taxable years beginning after December 31, 1966, by limiting the availability of the exclusion to dividends which are effectively connected with the conduct of a trade or business in the United States. The exclusion is also allowed in the case of an expatriate subject to tax under new section 877.

e. Withholding of tax on nonresident alien individuals (secs. 103(h) and (k) of the act and secs. 1441 and 3401 of the code)

Prior law.—Prior law generally required the withholding of tax in the case of a nonresident alien on U.S. source fixed or determinable income from U.S. sources (of the types previously described). The withholding was at a 30-percent rate (except in the case of certain treaty rates) and applied whether or not the flat 30-percent tax applied to the individual.² Thus it applied not only in the case of a nonresident alien with a gross income of \$21,200 or less who was not engaged in a trade or business in the United States but also in the case of a nonresident alien with a larger gross income or to one who was engaged in a trade or business in the United States.

Explanation of provisions.—The act adds a new provision to the existing nonresident alien withholding provisions. Under the new provision, withholding is not required on payments to nonresident

² For a limited category of scholarship and fellowship income and related income the withholding rate was 14 percent.