Title 50—Wildlife and Fisheries

CHAPTER I—U.S. FISH AND WILDLIFE SERVICE, DEPARTMENT OF THE INTERIOR

PART 28—PUBLIC ACCESS, USE, AND RECREATION

Blackwater National Wildlife Refuge, Maryland

The following special regulations are issued and are effective during the period January 1, 1975 through December 31, 1975.

§ 28.28 Special regulations, public access, use, and recreation; for individual wildlife refuge areas.

MARYLAND

BLACKWATER NATIONAL WILDLIFE REFUGE

Entry by foot or motor vehicle is permitted during daylight hours on designated travel routes for the purposes of nature study, photography, hiking, and sightseeing. Two-wheel motor vehicles (motorcycles, motorbikes, trail bikes, and mini-bikes) are not permitted on the auto drive. Visitors must remain in their vehicles while on the auto drive. Bicycles are permitted on a designated portion of the auto drive.

Pets are permitted on a leash not exceeding 10 feet in length in designated parking areas only.

Fires are prohibited for any purpose in the public use areas.

The refuge, comprising approximately 11,627 acres, is delineated on a map available from the Refuge Manager, Blackwater National Wildlife Refuge, Route 1, Box 121, Cambridge, Maryland 21613, or from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern recreation on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 28, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29773 Filed 12-20-74;8:45 am]

PART 28—PUBLIC ACCESS, USE, AND RECREATION

Montezuma National Wildlife Refuge, New York

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 28.28 Special regulations, public access, use, and recreation; for individual wildlife refuge areas.

NEW YORK

MONTEZUMA NATIONAL WILDLIFE REFUGE

Travel by motor vehicle or on foot is permitted on designated travel routes for the purpose of nature study, photography, and sight-seeing during daylight hours. Pets are permitted if on a leash not over 10 feet in length.

The refuge area, comprising 6,433 acres, is delineated on maps available from the Refuge Manager, Montezuma National Wildlife Refuge, R.D. #1, Box 1411, Seneca Falls, New York 13148 and from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern recreation on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 28, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29775 Filed 12-20-74;8:45 am]

PART 28—PUBLIC ACCESS, USE, AND RECREATION

Supawna Meadows National Wildlife Refuge, New Jersey

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 28.28 Special regulations, public access, use, and recreation; for individual wildlife refuge areas.

NEW JERSEY

SUPAWANA MEADOWS NATIONAL WILDLIFE REFUGE

Travel by bicycle or on foot is permitted from sunrise to sunset unless prohibited by posting, for the purpose of nature study, photography, hiking, and sight-seeing. Pets are permitted if on a leash not over ten feet in length.

The refuge area, comprising 653 acres, is delineated on maps available at refuge headquarters, Brigantine National Wildlife Refuge, PO. Box 72, Great Creek Road, Oceanville, new Jersey 08231, or from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern recreation on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 28, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29771 Filed 12-20-74;8:45 am]

PART 28—PUBLIC ACCESS, USE, AND RECREATION

Tinicum National Environmental Center, Pennsylvania

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 28.28 Special regulations, public access, use, and recreation; for individual wildlife refuge areas.

PENNSYLVANIA

TINICUM NATIONAL ENVIRONMENTAL CENTER

Entrance into the refuge is permitted for the purpose of bicycling, hiking, nature study, sightseeing and photography from dawn to dusk. Motorcycles, snowmobiles, all terrain, air cushion or other similar motor vehicles are prohibited on the refuge dikes. Pets are permitted if on a leash not exceeding 10 feet in length. Boats are not permitted in the refuge impoundments.

A map of the refuge is available at the refuge headquarters and from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse Building, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern recreation on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 28, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29772 Filed 12-20-74;8:45 am]

PART 28—PUBLIC ACCESS, USE, AND RECREATION

Trustom Pond National Wildlife Refuge, Rhode Island

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 28.28 Special regulations, public access, use, and recreation; for individual wildlife refuge areas.

RHODE ISLAND

TRUSTOM POND NATIONAL WILDLIFE REFUGE

Entry into and travel by bicycle or on foot is permitted from sunrise to sunset on designated routes unless prohibited by posting for the purpose of nature study, biking, photography, and sightseeing. Pets are permitted if on a leash not over 10 feet in length.

The entire refuge beach has no lifeguards. Swimming will be at the visitor's own risk. Year round access across the refuge for surf fishing is permitted.

Small cooking fires are permitted only on the ocean beach. No other fires are permitted at other locations on the refuge. Camping, tents, floating devices and nudity are not permitted on the refuge.

Over-the-sand vehicles, snowmobiles, air cushion, all terrain or other similar vehicles are not permitted on the refuge.

A map of the refuge is available from the Refuge Manager, Ninigret National Wildlife Refuge, Box 307, Charlestown, Rhode Island 02813 or from the Regional

Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations governing recreation on wildlife refuge areas generally, which are set forth in 50 CFR Part 28 and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29774 Filed 12-20-74;8:45 am]

PART 33—SPORT FISHING

Blackwater National Wildlife Refuge, Maryland

The following special regulations are issued and are effective during the period April 15, 1975 through October 31, 1975.

§ 33.5 Special regulations; sport fishing; for individual wildlife refuge areas.

MARYLAND

BLACKWATER NATIONAL WILDLIFE REFUGE

Sport fishing and crabbing on the Blackwater National Wildlife Refuge, Route 1, Box 121, Cambridge, Maryland 21613, is permitted only on those areas designated by signs as open to fishing. These open areas, comprising, approximately 2,700 acres, are delineated on a map available at refuge headquarters or from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109. Sport fishing and crabbing shall be in accordance with all applicable State regulations except for the following special conditions.

(1) Season: April 15–October 31—daylight hours only.

(2) Boat launching from refuge lands is not permitted.

(3) All fish and crab lines must be attended. No set tackle may be used.

(4) Use of airboats is prohibited.

The provisions of this special regulation supplement the regulations which govern sport fishing on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 33, and are effective through October 31, 1975

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29768 Filed 12-20-74;8:45 am]

PART 33—SPORT FISHING

Bombay Hook National Wildlife Refuge, Delaware

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 33.5 Special regulations; sport fishing; for individual wildlife refuge areas.

DELAWARE

BOMBAY HOOK NATIONAL WILDLIFE REFUGE

Sport fishing on the Bombay Hook National Wildlife Refuge, Smyrna, Delaware, is permitted in tidal waters. These open areas are delineated on maps available at refuge headquarters and from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse Building, Boston, Massachusetts 02109. Sport fishing shall be in accordance with all applicable State regulations subject to the following special conditions:

(1) Fishing from boats only is permitted.

The provisions of this special regulation supplement the regulations which govern fishing on wildlife refuge areas, generally, which are set forth in Title 50, Code of Federal Regulations, Part 33, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29770 Filed 12-20-74;8:45 am]

PART 33—SPORT FISHING

Iroquois National Wildlife Refuge, New York

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 33.5 Special regulation; sport fishing; for individual wildlife refuge areas.

NEW YORK

IROQUOIS NATIONAL WILDLIFE REFUGE

Sport fishing on the Iroquois National Wildlife Refuge, Basom, New York is permitted on all waters designated by signs as open in accordance with specified dates. Sport fishing shall be in accordance with all applicable State regulations subject to the following special conditions.

(1) All waters will be closed to fishing from April 1 through July 15 and October 1 through November 30 except those portions of the Feeder Canal and Oak Orchard Creek designated by signs as open.

(2) Boats without motors may be used on Oak Orchard Creek from the Knowlesville Road to a wire two miles westward.

(3) Firearms are not permitted in boats.

(4) Leaving boats, structures, or other equipment overnight on the refuge is not permitted.

All fishing areas are delineated on maps available at refuge headquarters or from the Regional Director, Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern fishing on wildlife refuge areas, generally, which are set forth in Title 50, Code of Federal Regulations, Part 33, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29767 Filed 12-20-74;8:45 am]

PART 33—SPORT FISHING

Prime Hook National Wildlife Refuge

The following special regulation is issued and is effective during the period January 1, 1975 through December 31, 1975.

§ 33.5 Special regulations; sport fishing; for individual wildlife refuge areas.

DELAWARE

PRIME HOOK NATIONAL WILDLIFE REFUGE

Sport fishing is permitted in accordance with all applicable State regulations. Boats, with or without motors, are permitted for fishing freshwater streams and ponds. Boats may be launched from designated access points or public roads.

The refuge is delineated on maps available at refuge headquarters or from the Regional Director, U.S. Fish and Wildlife Service, John W. McCormack Post Office and Courthouse, Boston, Massachusetts 02109.

The provisions of this special regulation supplement the regulations which govern fishing on wildlife refuge areas generally, which are set forth in Title 50, Code of Federal Regulations, Part 33, and are effective through December 31, 1975.

RICHARD E. GRIFFITH,
Regional Director, U.S. Fish and Wildlife Service.

DECEMBER 13, 1974.

[FR Doc.74-29769 Filed 12-20-74;8:45 am]

Title 26—Internal Revenue

CHAPTER I—INTERNAL REVENUE SERVICE, DEPARTMENT OF THE TREASURY

SUBCHAPTER A—INCOME TAX

[T.D. 7334]

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

Special Rules for Determining Tax Credit for Foreign Income Taxes Paid by Controlled Foreign Corporations

By a notice of proposed rule making appearing in the FEDERAL REGISTER for December 23, 1971 (36 FR 24816), amendments to the Income Tax Regulations (26 CFR Part 1) were proposed in order to provide special rules for determining the tax credit of a domestic corporation for foreign income taxes paid by a controlled foreign corporation. After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed, certain changes were made, and the proposed amendments of the regulations, subject to the changes indicated below, are adopted by this document.

Sections 1.960-1(c)(3) and 1.960-1(c)(2) have each been changed from the notice of proposed rule making by inserting a cross reference to the principles of paragraphs (b)(3) (iv) and (viii) and (c) of § 1.9541 for determining the effective foreign tax rate and by the addition of a simple example involving the dividends-received deduction.

This document also amends example (2) in § 1.963-3(h), which was amended by paragraph 9 of T.D. 7120, which was published in the FEDERAL REGISTER for June 4, 1971 (36 FR 10851). This amendment was not proposed with the notice of proposed rule making published on December 23, 1971. The penultimate sentence in example (2) provides that the foreign tax credit is determined in accordance with § 1.963-4. This is incorrect since the example does not involve a chain or group of controlled foreign corporations. Accordingly, the sentence has been corrected to refer to section 902 as modified by the regulations under section 963.

The proposed amendments of the regulations are hereby adopted, subject to the changes set forth below, effective for taxable years of foreign corporations beginning after December 31, 1962, and for taxable years of U.S. shareholders within which or with which such taxable years of such corporations end:

PARAGRAPH 1. The amendment of § 1.960-1, as set forth in paragraph 2 of the notice, is changed by revising so much of § 1.960-1 (c) (3) as follows subdivision (ii) thereof to read as set forth below.

PAR. 2. The amendment of § 1.960-2, as set forth in paragraph 3 of the notice, is changed by revising so much of § 1.960-2 (c) (2) as follows subdivision (ii) thereof to read as set forth below.

Par. 3. Section 1.963-3 is amended by revising example (2) in paragraph (h) to read as set forth below.

(Sec. 7805, Internal Revenue Code of 1954 (68A Stat. 917 (26 U.S.C. 7805)))

[SEAL] DONALD C. ALEXANDER,
Commissioner of Internal Revenue.

Approved: December 16, 1974.

FREDERIC W. HICKMAN,
Assistant Secretary of the Treasury.

1. In § 1.959-3 paragraph (e) is amended to read as follows:

§ 1.959-3 Allocation of distributions to earnings and profits of foreign corporations.

* * * * *

(e) *Determination of foreign tax credit.* For purposes of applying section 902 and section 960 in determining the foreign tax credit allowable under section 901 in a case in which distributions are made by a second-tier corporation or a first-tier corporation, as the case may be, from its earnings and profits for a taxable year which are attributable to an amount included in the gross income of a U.S. shareholder under section 951(a) or which are attributable to amounts excluded from the gross income of such foreign corporation under section 959(b) and § 1.959-2 with respect to a U.S. shareholder, the rules of paragraph (b) of this section shall apply except that in applying subparagraph (1) or (2) of such paragraph—

(1) Distributions from the earnings and profits for such taxable year of the second-tier corporation shall be considered first attributable to its earnings and profits attributable to distributions from the earnings and profits of the foreign corporation, if any, next lower in the chain of ownership described in section 958(a), to the extent of such earnings and profits of the second-tier corporation, and then to the other earnings and profits of such second-tier corporation, and

(2) Distributions from the earnings and profits for such taxable year of the first-tier corporation shall be considered first attributable to its earnings and profits attributable to distributions from the earnings and profits of the second-tier corporation, to the extent of such earnings and profits of the first-tier corporation, and then to the other earnings and profits of such first-tier corporation. For purposes of this paragraph, a second-tier corporation is a foreign corporation referred to in section 960(a)(1)(B), and a first-tier corporation is a foreign corporation referred to in section 960 (a)(1)(A). The application of this paragraph may be illustrated by the following examples:

Example (1) * * *

(c) During 1964, S Corporation distributes $100 to R Corporation, and R Corporation distributes $100 to A Corporation. Neither corporation has any earnings or profits or deficit in earnings and profits for such year. On December 31, 1964, R Corporation has earnings and profits (computed before distributions to A Corporation made for the year) of $200, consisting of $100 of section 959 (c)(1) amounts of R Corporation for 1963 and of $100 of section 959(c)(1) amounts of S Corporation for 1963. For purposes of determining the foreign tax credit under section 960 and the regulations thereunder, the $100 distribution by R Corporation shall be considered attributable to S Corporation's earnings and profits for 1963 described in section 959 (c)(1).

Example (2). * * *

(c) During 1965 neither T Corporation nor U Corporation has any earnings and profits or deficit in earnings and profits or investment of earnings in U.S. property, but T Corporation distributes $100 to A Corporation. For purposes of determining the foreign tax credit under section 960 and the regulations thereunder, the $100 distribution of T Corporation shall be considered attributable to T Corporation's earnings and profits for 1964 described in section 959(c)(1).

* * * * *

2. In § 1.960-1 paragraph (c) is amended to read as follows:

§ 1.960-1 Foreign tax credit with respect to taxes paid on earnings and profits of controlled foreign corporations.

* * * * *

(c) *Amount of foreign income taxes deemed paid by domestic corporation in respect of earnings and profits of foreign corporation attributable to amount included in income under section 951*—(1) *In general.* * * *

(iii) In applying subdivision (i) of this subparagraph to a first-tier corporation which for the taxable year has income excluded under section 959(b), subparagraph (3) of this paragraph shall apply for purposes of excluding certain earnings and profits of such corporation and foreign income taxes, if any, attributable to such excluded income.

* * * * *

(3) *Exclusion of earnings and profits and taxes of first-tier corporation having income excluded under section 959(b).* If in the case of a first-tier corporation to which subparagraph (1)(i) of this paragraph is applied—

(i) The earnings and profits of such first-tier corporation for its taxable year consist of (*a*) earnings and profits attributable to dividends received from a second-tier corporation to which, in accordance with paragraph (b) of § 1.960-2, section 902(b) does not apply and (*b*) other earnings and profits, and

(ii) The effective rate of foreign income taxes paid or accrued by such first-tier corporation in respect to the dividends to which its earnings and profits described in subdivision (i)(*a*) of this subparagraph are attributable is higher or lower than the effective rate of foreign income taxes paid or accrued by such first-tier corporation in respect to the income to which its earnings and profits described in subdivision (i)(*b*) of this subparagraph are attributable, then, for purposes of applying subparagraph (1)(i) of this paragraph to the foreign income taxes paid, accrued, or deemed to be paid, by such first-tier corporation on or with respect to its earnings and profits for such taxable year, the earnings and profits of such first-tier corporation for such taxable year shall be considered not to include the earnings and profits described in subdivision (i)(*a*) of this subparagraph and only the foreign income taxes paid, accrued, or deemed to be paid, by such first-tier corporation in respect to the income to which its earnings and profits described in subdivision (i)(*b*) of this subparagraph are attributable shall be taken into account. For purposes of applying this subparagraph, the effective rate of foreign income taxes paid or accrued in respect to income shall be determined consistently with the principles of paragraphs (b)(3)(iv) and (viii) and (c) of

§ 1.954–1. Thus, for example, the effective rate of foreign income taxes paid or accrued in respect to dividends received by such first-tier corporation shall be determined by taking into account any intercorporate dividends received deduction allowed to such corporation for such dividends.

(4) *Illustrations*. * * *

Example (6). Domestic corporation N owns all the one class of stock of controlled foreign corporation A, not a less developed country corporation, which owns all one class of stock of controlled foreign corporation B. All such corporations use the calendar year as the taxable year. For 1965, N Corporation is required under section 951 to include in gross income $175 attributable to the earnings and profits of A Corporation for such year. For 1965, B Corporation has earnings and profits of $225, on which it pays foreign income taxes of $75. In 1965, B Corporation distributes $150, which, under paragraph (b) of § 1.960–2, consists of $100 to which section 902(b) does not apply (from B Corporation's earnings and profits attributable to an amount required under section 951 to be included in N Corporation's gross income with respect to B Corporation) and $50 to which section 902(b)(1) applies (from B Corporation's other earnings and profits). The country under the laws of which A Corporation is incorporated imposes an income tax of 40 percent on all income but exempts from tax dividends received from a subsidiary corporation. A Corporation makes no distribution for 1965. Under paragraph (b) of § 1.960–2, A Corporation is deemed to have paid $25 ($50/$150 × $75) of the $75 foreign income taxes paid by B Corporation on its pretax earnings and profits of $225. The foreign income taxes deemed paid by N Corporation for 1965 under section 960(a)(1)(C) with respect to A Corporation are determined as follows upon the basis of the following assumed facts:

Pretax earnings and profits of A corporation:	
Dividends received from B corporation	$150.00
Other income	250.00
Total pretax earnings and profits	400.00
Foreign income taxes:	
On dividends received from B corporation	None
On other income ($250×0.40)	100.00
Total foreign income taxes	100.00
Earnings and profits:	
Attributable to dividends received from B corporation to which sec. 902(b) does not apply	100.00
Attributable to other income:	
Attributable to dividends received from B corporation to which section 902(b)(1) applies	50.00
Attributable to other income ($250—$100 [$250×0.40])	150.00
Subtotal	200.00
Total earnings and profits	300.00
Foreign income taxes deemed paid by N corporation under sec. 960(a)(1)(C) with respect to A corporation:	
Tax paid by A corporation in respect to its income other than dividends received from B corporation to which sec. 902(b) does not apply ($175/$200×$100)	87.50
Tax of B corporation deemed paid by A corporation under sec. 902(b)(1) in respect to such income ($175/$200×$25)	21.88
Total foreign income taxes deemed paid by N corporation under sec. 960(a)(1)(C) with respect to A corporation	109.38

3. In § 1.960–2 paragraphs (c) and (e) are amended to read as follows:

§ 1.960–2 Interrelation of section 902 and section 960 when dividends are paid by second-tier corporation or by first-tier corporation.

* * * * *

(c) *Application of section 902(a) to dividends received by domestic corporation from first-tier corporation*. * * *

(2) *Separate determinations under section 902(a) in case of first-tier corporation having income excluded under section 959(b)*. If in the case of a first-tier corporation to which subparagraph (1) of this paragraph is applied—

(i) The earnings and profits of such first-tier corporation for its taxable year consist of (*a*) earnings and profits attributable to dividends received from a second-tier corporation to which, in accordance with paragraph (b) of this section, section 902(b) does not apply and (*b*) other earnings and profits, and

(ii) The effective rate of foreign income taxes paid or accrued by such first-tier corporation in respect to the dividends to which its earnings and profits described in subdivision (i)(*a*) of this subparagraph are attributable is higher or lower than the effective rate of foreign income taxes paid or accrued by such first-tier corporation in respect to the income to which its earnings and profits described in subdivision (i)(*b*) of this subparagraph are attributable, then, for purposes of applying subparagraph (1) of this paragraph to dividends received by the domestic corporation from the first-tier corporation, section 902(a) shall be applied separately to the portion of the dividends which is attributable to the earnings and profits described in subdivision (i)(*a*) of this subparagraph and separately to the portion of the dividends which is attributable to the earnings and profits described in subdivision (i)(*b*) of this subparagraph. For this purpose, in making each such separate determination, only the foreign income taxes paid, accrued, or, in the case of earnings and profits described in subdivision (i)(*b*) of this subparagraph, deemed to be paid, by such first-tier corporation in respect to the income to which the earnings and profits are attributable in respect of which the separate determination is being made shall be taken into account. For purposes of applying this subparagraph, no part of the foreign income taxes paid, accrued, or deemed to be paid, by such first-tier corporation for such taxable year in respect to the income to which its earnings and profits described in subdivision (i)(*b*) of this subparagraph are attributable shall be attributed to its earnings and profits described in subdivision (i)(*a*) of this subparagraph; and no part of the foreign income taxes paid or accrued by such first-tier corporation for such taxable year in respect to the dividends to which its earnings and profits described in subdivision (i)(*a*) of this subparagraph are attributable shall be attributed to its earnings and profits described in subdivision (i)(*b*) of this subparagraph. Furthermore, the effective rate of foreign income taxes paid or accrued in respect to income shall be determined consistently with the principles of paragraphs (b)(3)(iv) and (viii) and (c) of § 1.954–1. Thus, for example, the effective rate of foreign income taxes paid or accrued in respect to dividends received by such first-tier corporation shall be determined by taking into account any intercorporate dividends received deduction allowed to such corporation for such dividends.

* * * * *

(e) *Illustrations*. The application of this section may be illustrated by the following examples, in all of which, other than examples (7) and (8), it is assumed that the effective rate of foreign income taxes paid or accrued by the first-tier corporation in respect to dividends received from the second-tier corporation is the same as the effective rate of foreign income taxes paid or accrued by the first-tier corporation in respect to its other income:

* * * * *

Example (7). Domestic corporation N owns all the one class of stock of controlled foreign corporation A, not a less developed country corporation, which owns all the one class of stock of controlled foreign corporation B. All such corporations use the calendar year as the taxable year. For 1965, N Corporation is required under section 951 to include in gross income $100 attributable to the earnings and profits of B Corporation for such year. For 1965, B Corporation distributes $150 consisting of $100 from its earnings and profits attributable to the amount required under section 951 to be included in N Corporation's gross income with respect to B Corporation and $50 from its other earnings and profits. The country under the laws of which A Corporation is incorporated imposes an income tax of 10 percent on all income but exempts from tax dividends received from a subsidiary corporation. For 1965, A Corporation distributes $175, consisting of $100 from its earnings and profits attributable to the amount required under section 951 to be included in N Corporation's gross income with respect to B Corporation, and $75 from its other earnings and profits. The foreign income taxes deemed paid by N Corporation for 1965 under section 960(a)(1)(C) and section 902(a)(1) are determined as follows on the basis of the facts assumed:

B corporation (2d-tier corporation):	
Pretax earnings and profits	$200.00
Foreign income taxes (20%)	40.00
Earnings and profits	160.00
Amount required to be included in N corporation's gross income for 1965 under sec. 951 with respect to B corporation	100.00
Dividends paid by B corporation:	
Dividends to which sec. 902(b) does not apply (from B corporation's earnings and profits in respect of which an amount is required under sec. 951 to be included in N corporation's gross income with respect to B corporation)	100.00
Dividends to which sec. 902(b)(1) applies (from B corporation's other earnings and profits)	50.00
Total dividends paid to A corporation	150.00
Foreign income taxes of B corporation deemed paid by A corporation for 1965 under sec. 902(b)(1) ($50/$100×$40)	12.50
A corporation (1st-tier corporation):	
Pretax earnings and profits:	
Dividends received from B corporation	150.00
Other income	100.00
Total pretax earnings and profits	250.00
Foreign income taxes:	
On dividends received from B corporation	None
On other income ($100×0.10)	10.00
Total foreign income taxes	10.00
Earnings and profits:	
Attributable to dividends received from B corporation to which sec. 902(b) does not apply	100.00
Attributable to other income:	
Attributable to dividends received from B corporation to which sec. 902(b)(1) applies	50.00
Attributable to other income ($100−$10)	90.00
Subtotal	140.00
Total earnings and profits	240.00
Earnings and profits after exclusion of amounts attributable to dividends to which sec. 902(b) does not apply ($240−$100)	140.00
Amount required to be included in N corporation's gross income for 1965 under sec. 951 with respect to A corporation	None
Dividends paid by A corporation:	
Dividends to which sec. 902(a) does not apply (from A corporation's earnings and profits in respect of which an amount is required under sec. 951 to be included in N corporation's gross income with respect to A corporation)	None
Dividends to which sec. 902(a)(1) applies (from A corporation's other earnings and profits)	175.00
Total dividends paid to N corporation	175.00
N corporation (domestic corporation):	
Foreign income taxes deemed paid by N corporation under sec. 960(a)(1)(C) with respect to B corporation ($100/$160×$40)	25.00
Foreign income taxes deemed paid by N corporation under sec. 902(a)(1) with respect to A corporation (allocation of earnings and profits being made under pars. (c)(2) and (d) of this section):	
Tax paid by A corporation in respect to dividends received from B corporation to which sec. 902(b) does not apply ($100/$100×$0)	None
Tax paid by A corporation in respect to its other income ($75/$140×$10)	5.36
Tax of B corporation deemed paid by A corporation in respect to such other income ($75/$140×$12.50)	6.70
Total taxes deemed paid under sec. 902(a)(1)	12.06
Total foreign income taxes deemed paid by N corporation under sec. 901	37.06

Example (8). Domestic corporation N owns all the one class of stock of controlled foreign corporation A, not a less developed country corporation, which owns all the one class of stock of controlled foreign corporation B. All such corporations use the calendar year as the taxable year. For 1965, N Corporation is required under section 951 to include in gross income $150 attributable to the earnings and profits of B Corporation for such year and $47.50 attributable to the earnings and profits of A Corporation for such year. For 1965, B Corporation distributes $200, consisting of $150 from its earnings and profits attributable to the amount required under section 951 to be included in N Corporation's gross income with respect to B Corporation and $50 from its other earnings and profits. The country under the laws of which A Corporation is incorporated imposes an income tax of 5 percent on dividends received from a subsidiary corporation and 20 percent on other income. For 1965, A Corporation distributes $100 from its earnings and profits to N Corporation, such amount being attributable under paragraph (e) of § 1.959–3 to the amount required under section 951 to be included in N Corporation's gross income with respect to B Corporation. The foreign income taxes deemed paid by N Corporation for 1965 under section 960(a)(1)(C) and section 902(a)(1) are determined as follows on the basis of the facts assumed:

B corporation (2d-tier corporation):	
Pretax earnings and profits	$250.00
Foreign income taxes (20 percent)	50.00
Earnings and profits	200.00
Amount required to be included in N corporation's gross income for 1965 under sec. 951 with respect to B corporation	150.00
Dividends paid by B corporation:	
Dividends to which sec. 902(b) does not apply (from B corporation's earnings and profits in respect of which an amount is required under sec. 951 to be included in N corporation's gross income with respect to B corporation)	150.00
Dividends to which sec. 902(b)(1) applies (from B corporation's other earnings and profits)	50.00
Total dividends paid to A corporation	200.00
Foreign income taxes of B corporation deemed paid by A corporation for 1965 under sec. 902(b)(1) ($50/$200×$50)	12.50
A corporation (1st-tier corporation):	
Pretax earnings and profits:	
Dividends received from B corporation	200.00
Other income	100.00
Total pretax earnings and profits	300.00
Foreign income taxes:	
On dividends received from B corporation to which sec. 902(b) does not apply ($150×0.05)	7.50
On other income:	
Dividends received from B corporation which to sec. 902(b)(1) applies ($50×0.05)	2.50
Other income of A corporation ($100×0.20)	20.00
Total	22.50
Total foreign income taxes	30.00
Earnings and profits:	
Attributable to dividends received from B corporation to which sec. 902(b) does not apply ($150—$7.50)	142.50
Attributable to other income:	
Attributable to dividends received from B corporation to which sec. 902(b)(1) applies ($50—$2.50)	47.50
Attributable to other income ($100—$20)	80.00
Total	127.50
Total earnings and profits	270.00
Earnings and profits after exclusion of amounts attributable to dividends to which sec. 902(b) does not apply ($270 less $142.50)	127.50
Amount required to be included in N corporation's gross income for 1965 under sec. 951 with respect to A corporation	47.50
Dividends paid by A corporation:	
Dividends to which sec. 902(a) does not apply (from A corporation's earnings and profits in respect of which an amount is required under sec. 951 to be included in N corporation's gross income with respect to A corporation)	None
Dividends to which sec. 902(a)(1) applies (from A corporation's other earnings and profits)	100.00
Total dividends paid to N corporation	100.00
N Corporation (domestic corporation):	
Foreign income taxes deemed paid by N corporation under sec. 960(a)(1)(C) with respect to—	
B corporation ($150/$200×$50)	37.50
A corporation (allocation of earnings and profits being made under § 1.960-1(c) (3) and par. (d) of this sec.):	
Tax paid by A corporation ($47.50/$127.50×$22.50)	8.38
Tax of B corporation deemed paid by A corporation under sec. 902(b)(1) ($47.50/$127.50×$12.50)	4.66
Total	13.04
Total taxes deemed paid under sec. 960(a)(1)(C)	50.54
Foreign income taxes deemed paid by N corporation under sec. 902(a)(1) with respect to A corporation (allocations of earnings and profits being made under pars. (c)(2) and (d) of this sec.) ($100/$142.50×$7.50)	5.26
Total foreign income taxes deemed paid by N Corporation under sec. 901	55.80

4. In § 1.963-3 paragraph (h) is amended to read as follows:

§ 1.963-3 Distributions counting toward a minimum distribution.

* * * * *

(h) *Illustrations*. The application of this section may be illustrated by the following examples:

* * * * *

Example (2). Domestic corporation M directly owns all of the one class of stock of controlled foreign corporation A. Both corporations use the calendar year as the taxable year, and A Corporation's taxable year and its distribution period for 1963 coincide. For 1963, $50 is included in the gross income of M Corporation under section 951(a)(1)(B) as A Corporation's increase in earnings invested for such year in United States property. For 1964, M Corporation makes a first-tier election with respect to A Corporation. For 1964, A Corporation has earnings and profits of $100, including $10 attributable to an increase in earnings invested for such year in United States property. During 1964, A Corporation distributes earnings and profits of $80 to M Corporation. Without regard to paragraph (e) of this section, $10 of this distribution is attributable under section 959(c)(1) to A Corporation's 1964 earnings and profits required to be included in M Corporation's gross income under section 951(a)(1)(D). Pursuant to paragraph (e) of this section, however, the entire distribution of $80 counts toward a minimum distribution for 1964 and is considered to be from earnings and profits of A Corporation for 1964 described in section 959(c)(3). Thus the entire distribution of $80 is included in M Corporation's gross income as a dividend and the foreign tax credit in respect of such amount is determined in accordance with section 902 as modified by the regulations under section 963. On the other hand, if A Corporation made no distributions for 1964, no part of the $10 of A Corporation's increase in earnings invested in United States property for such year would count toward a minimum distribution for any other year but would be included in the gross income for M Corporation for 1964 under section 951(a)(1)(B), and the foreign tax credit in respect of such amount would be determined in accordance with § 1.960-1.

* * * * *

[FR Doc.74-29867 Filed 12-20-74;8:45 am]

[TD 7332]

PART 1—INCOME TAX; TAXABLE YEARS BEGINNING AFTER DECEMBER 31, 1953

SUBCHAPTER F—PROCEDURE AND ADMINISTRATION

PART 301—PROCEDURE AND ADMINISTRATION

Imposition of Tax on Nonresident Alien Individuals; Return Requirements; Declarations of Estimated Income Tax

By a notice of proposed rule making appearing in the FEDERAL REGISTER for October 5, 1971 (36 FR 19371), amendments to the Income Tax Regulations (26 CFR Part 1) and the regulations on procedure and administration (26 CFR Part 301) were proposed in order to conform such regulations to the amendments of the Internal Revenue Code of 1954 made by subsections (a), (b), (f), (g), (j), (l), and (m) of section 103 of the Foreign Investors Tax Act of 1966 (80 Stat. 1547, 1550, 1551, 1552, and 1554). The amendments made by such subsections are effective for taxable years beginning after December 31, 1966.

Section 103(a) of the Act amends section 871 of the Code to substantially revise the income tax treatment of nonresident alien individuals. Under the new provisions the income of a nonresident alien individual which is effectively connected with the conduct of a U.S. business is taxed at the regular graduated rates applicable to individuals, and certain income from U.S. sources which is not so connected is taxed at a flat 30-percent rate. U.S. source capital gains of a nonresident alien individual not engaged in business in the United States are taxed at a flat rate of 30 percent, but only if the alien was in the United States for 183 days or more during the taxable year. An election is also provided which allows a nonresident alien individual to treat income from real property as income which is effectively connected with the conduct of a U.S. business. Moreover, a new rule provides for an exclusion from gross income of certain annuities received under qualified stock bonus, pension, profit-sharing, or annuity plans in certain circumstances.

Section 103(b) of the Act adds a new rule in section 872 of the Code that the gross income of a nonresident alien individual includes only that income from U.S. sources which is not effectively connected with the conduct of a U.S. business and all income (whether or not derived from U.S. sources) which is effectively connected with the conduct of a U.S. business. A new section 872(b)(4) excludes from gross income certain bond income of residents of certain Pacific Islands.

Section 103(f) of the Act adds to the Code a new section 877, which provides in certain cases for a special income tax in the case of an individual who at any time after March 8, 1965, and within the 10-year period preceding the close of the taxable year made a tax-motivated expatriation from the United States.

Section 103(g) of the Act amends 116 of the Code to provide that, in the case of a nonresident alien individual, the $100 dividend exclusion applies as a general rule only in determining the graduated tax and only if the dividends are effectively connected with the conduct of a U.S. business.

Section 103(j) of the Act adds a new section 6015(i) to the Code. Under new section 6015(i) a declaration of estimated tax is required of a nonresident alien individual only if he is subject to withholding of tax on wages, or has certain income which is effectively connected with the conduct of a U.S. business, or is a resident of Puerto Rico for the entire taxable year.

Section 103(l) of the Act makes what is essentially a conforming amendment in 7701(a)(31) of the Code, relating to the definition of a foreign estate or trust.

Section 103(m) of the Act makes a conforming amendment in section 932 of the Code, relating to citizens of possessions of the United States who are not otherwise citizens of the United States.

In addition to conforming the regulations to the changes made by the Foreign Investors Tax Act of 1966 certain other changes are made in the Income Tax Regulations. Thus, new § 1.871-13 provides rules for the taxation of an alien individual for a taxable year in which he becomes a citizen or resident of the United States or of an individual for a taxable year in which he gives up his U.S. citizenship or becomes a nonresident alien. An amendment to § 1.932-1(a)(1) incorporates a rule, taken in principle form I.T. 3788, 1946-1 C.B. 153, that the term "naturalization", as used in such section, means only naturalization in a State, Territory, or the District of Columbia. Section 1.6012-1(b) contains revised return requirements of nonresident alien individuals. One significant change is that with certain exceptions every nonresident alien individual who is engaged in trade or business in the United States is required to make a return of income. Another change consists of return requirements in the case of an individual who becomes a citizen or resident of the United States, or abandons his U.S. citizenship or residence, during the taxable year.

In order to avoid confusion by making such amendments in the Income Tax Regulations as were necessary to conform to the significant changes made by the 1966 Act, the decision was reached to replace the pertinent regulations with completely new regulations applicable only to taxable years beginning after December 31, 1966, and to refer to those sections in the Code of Federal Regulations (revised as of January 1, 1971) where the corresponding rules for taxable years beginning before January 1, 1967, may be found.

After consideration of all such relevant matter as was presented by interested persons regarding the rules proposed on October 5, 1971, the amendments of the regulations as so proposed are hereby adopted, subject to the changes set forth below:

INCOME TAX REGULATIONS

PARAGRAPH 1. The amendment to § 1.1-1, as set forth in paragraph 2 of the notice of proposed rule making, is changed by adding thereto an amendment of so much of paragraph (a)(2) as precedes the table therein and by adding a new paragraph (a)(2)(ii), to read as set forth below.

PAR. 2. Section 1.871-1, as set forth in paragraph 10 of the notice of proposed rule making, is changed by revising paragraph (a) to read as set forth below.

PAR. 3. Section 1.871-7, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising paragraph (d)(3)(i) to read as set forth below.

PAR. 4. Section 1.871-8, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising paragraph (b)(1), example (2) in paragraph (c)(2), and paragraph (d) to read as set forth below.

PAR. 5. Section 1.871-10, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising paragraph (b)(3), and by adding a new subparagraph (3) to paragraph (d), to read as set forth below.

PAR. 6. Section 1.871-11, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising paragraphs (a), (c), and (e), and example (2)(a) in paragraph (f), to read as set forth below.

PAR. 7. Section 1.871-12, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising paragraph (c)(2) and example (2) in paragraph (d) to read as set forth below.

PAR. 8. Section 1.871-13, as set forth in paragraph 12 of the notice of proposed rule making, is changed by revising the heading of such section, by revising paragraphs (a), (b), (c), and (d), and by revising example (3) in paragraph (e), to read as set forth below.

PAR. 9. Section 1.872-2, as set forth in paragraph 16 of the notice of proposed rule making, is changed by revising paragraph (e)(2) to read as set forth below.

PAR. 10. Section 1.876-1, as set forth in paragraph 17 of the notice of proposed rule making, is changed by revising paragraph (c) to read as set forth below.

PAR 11. Section 1.878, as set forth in paragraph 18 of the notice of proposed rulemaking, is changed to read as set forth below.

PAR. 12. The amendment of § 1.932-1 (a)(1), as set forth in paragraph 21 of the notice of proposed rulemaking, is changed to read as set forth below.

PAR. 13. The amendment of § 1.6012-1, as set forth in paragraph 24 of the notice of proposed rulemaking, is changed by deleting the amendment of paragraph (a)(5) and by revising subparagraphs (1)(i), (2)(ii), (3)(ii), and (5) of paragraph (b) to read as set forth below.

PAR. 14. The amendment of § 1.6012-3, as set forth in paragraph 25 of the notice of proposed rulemaking, is changed by revising paragraph (b)(2)(i)(c) to read as set forth below.

PAR. 15. The amendment of § 1.6015 (a), as set forth in paragraph 27 of the notice of proposed rule making, is deleted.

PAR. 16. The amendment of § 1.6015 (a)-1, as set forth in paragraph 28 of the notice of proposed rule making, is changed by striking out the deletion of paragraph (c).

PAR. 17. Section 1.6015(i)-1, as set forth in paragraph 31 of the notice of proposed rule making, is changed by revising paragraph (b)(1) to read as set forth below.

PAR. 18. Section 1.703-1 is amended by adding at the end of paragraph (b)(2) the following new subdivision to read as set forth below.

PAR. 19. Section 1.864-4 is amended by revising paragraph (c)(3)(i) to read as set forth below.

PAR. 20. The following new section is added immediately after § 1.875-1 to read as set forth below.

PAR. 21. Section 1.912 is amended to read as set forth below.

PAR. 22. Section 1.6012-2 is amended by revising paragraph (g)(5) to read as set forth below.

REGULATIONS ON PROCEDURE AND ADMINISTRATION

PAR. 23. Section 301.6015 is amended by revising subsection (c) of section 6015, by redesignating subsection (i) of section 6015 as subsection (j), by adding a new subsection (i) to section 6015 immediately after subsection (h), and by revising the historical note, as set forth below.

PAR. 24. Section 301.6015-1 is amended to read as set forth below.

PAR. 25. Section 301.7701, as set forth in paragraph 33 of the notice of proposed rulemaking, is amended by revising paragraph (34)(B) of section 7701(a) and the historical note to read as set forth below.

(Sec. 7805 of the Internal Revenue Code of 1954 (68A Stat. 917; 26 U.S.C. 7805).)

[SEAL] DONALD C. ALEXANDER,
Commissioner of Internal Revenue.

Approved: December 16, 1974.

Frederic W. Hickman,
Assistant Secretary of the Treasury.

PARAGRAPH 1. Section 1.1 is amended by redesignating subsection (d) of section 1 (as amended by section 111 of the Revenue Act of 1964) as subsection (e), by adding a new subsection (d) to such section 1, and by revising the first historical note, as follows:

§ 1.1 Statutory provisions; tax imposed.

SECTION 1. *Tax imposed.* * * *

(d) *Nonresident aliens.* In the case of a nonresident alien individual, the tax imposed by subsection (a) shall apply only as provided by section 871 or 877.

(e) *Cross reference.* For definition of taxable income, see section 63.

[Sec. 1 as amended by sec. 111, Rev. Act 1964 (78 Stat. 19); sec. 103(a)(2), Foreign Investors Tax Act 1966 (80 Stat. 1550)]

* * * * *

PAR. 2. Section 1.1-1 is amended by revising paragraphs (a)(1), (b), and (c) to read as follows:

§ 1.1-1 Income tax on individuals.

(a) *General rule.* (1) Section 1 of the Code imposes an income tax on the income of every individual who is a citizen or resident of the United States and, to the extent provided by section 871(b) or 877(b), on the income of a nonresident alien individual. For optional tax in the case of taxpayers with adjusted gross income of less than $10,000 (less than $5,000 for taxable years beginning before January 1, 1970) see section 3. The tax imposed is upon taxable income (determined by subtracting the allowable deductions from gross income). The tax is determined in accordance with the table contained in section 1. See subparagraph (2) of this paragraph for reference guides to the appropriate table for taxable years beginning on or after January 1, 1964, and before January 1, 1965, taxable years beginning after December 31, 1964, and before January 1, 1971, and taxable years beginning after December 31, 1970. In certain cases credits are allowed against the amount of the tax. See part IV (section 31 and following), subchapter A, chapter 1 of the Code. In general, the tax is payable upon the basis of returns rendered by persons liable therefor (subchapter A (sections 6001 and following), chapter 61 of the Code) or at the source of the income by withholding. For the computation of tax in the case of a joint return of a husband and wife, or a return of a surviving spouse, for taxable years beginning before January 1, 1971, see section 2. The computation of tax in such a case for taxable years beginning after December 31, 1970, is determined in accordance with the table contained in section 1(a) as amended by the Tax Reform Act of 1969. For other rates of tax on individuals, see section 5(a). For the imposition of an additional tax for the calendar years 1968, 1969, and 1970, see section 51(a).

(2)(i) For taxable years beginning on or after January 1, 1964, the tax imposed upon a single individual, a head of a household, a married individual filing a separate return, and estates and trusts is the tax imposed by section 1 determined in accordance with the appropriate table contained in the following subsection of section 1:

* * * * *

(ii) For taxable years beginning after December 31, 1970, the tax imposed by section 1(d), as amended by the Tax Reform Act of 1969, shall apply to the income effectively connected with the conduct of a trade or business in the United States by a married alien individual who is a nonresident of the United States for all or part of the taxable year or by a foreign estate or trust. For such years the tax imposed by section 1(c), as amended by such Act, shall apply to the income effectively connected with the conduct of a trade or business in the United States by an unmarried alien individual (other than a surviving spouse) who is a nonresident of the United States for all or part of the taxable year. See paragraph (b)(2) of § 1.871-8.

* * * * *

(b) *Citizens or residents of the United States liable to tax.* In general, all citizens of the United States, wherever resident, and all resident alien individuals are liable to the income taxes imposed by the Code whether the income is received from sources within or without the United States. Pursuant to section 876, a nonresident alien individual who is a bona fide resident of Puerto Rico during ing the entire taxable year is, except as provided in section 933 with respect to Puerto Rican source income, subject to taxation in the same manner as a resident alien individual. As to tax on nonresident alien individuals, see sections 871 and 877.

(c) *Who is a citizen.* Every person born or naturalized in the United States and subject to its jurisdiction is a citizen. For other rules governing the acquisition of citizenship, see chapters 1 and 2 of title III of the Immigration and Nationality Act (8 U.S.C. 1401-1459). For rules governing loss of citizenship, see sections 349 to 357, inclusive, of such Act (8 U.S.C. 1481-1489), Schneider v. Rusk, (1964) 377 U.S. 163, and Rev. Rul. 70-506, C.B. 1970-2, 1. For rules pertaining to persons who are nationals but not citizens at birth, e.g., a person born in American Samoa, see section 308 of such Act (8 U.S.C. 1408). For special rules applicable to certain expatriates who have lost citizenship with a principal purpose of avoiding certain taxes, see section 877. A foreigner who has filed his declaration of intention of becoming a citizen but who has not yet been admitted to citizenship by a final order of a naturalization court is an alien.

PAR. 3. Section 1.116 is amended by revising section 116(d) and by revising the historical note. These amended provisions read as follows:

§ 1.116 Statutory provisions; partial exclusion of dividends received by individuals.

SEC. 116. *Partial exclusion of dividends received by individuals.* * * *

(d) *Certain nonresident aliens ineligible for exclusion.* In the case of a nonresident alien individual, subsection (a) shall apply only—

(1) In determining the tax imposed for the taxable year pursuant to section 871(b)(1) and only in respect of dividends which are effectively connected with the conduct of a trade or business within the United States, or

(2) In determining the tax imposed for the taxable year pursuant to section 877(b).

[Sec. 116 as amended by sec. 3(a), Life Insurance Company Tax Act 1959 (73 Stat. 139); sec. 10(f), Act of Sept. 14, 1960 (Public Law 86-779, 74 Stat. 1009); secs. 201 (c) and (d)(6)(C), Rev. Act 1964 (78 Stat. 32); sec. 103(g), Foreign Investors Tax Act 1966 (80 Stat. 1552)]

PAR. 4. Section 1.116-1 is amended by revising paragraph (e)(1). This amended provision reads as follows:

§ 1.116-1 Partial exclusion of dividends.

* * * * *

(e) *Taxpayers not entitled to exclusion.* (1) For taxable years beginning after December 31, 1966, the exclusion allowed by section 116(a) and paragraph (a) of this section shall, in the case of a nonresident alien individual, apply only (i) in determining the tax imposed for the taxable year pursuant to section 871(b)(1), and the regulations thereunder, and only in respect of dividends which are effectively connected for the taxable year with the conduct of a trade or business in the United States by such individual, or (ii) in determining the tax imposed for the taxable year pursuant to section 877(b). For taxable years beginning before January 1, 1967, the exclusion is not available to nonresident alien individuals with respect to whom a tax is imposed for the taxable year under section 871(a).

* * * * *

PAR. 5. Section 1.154 is amended by revising section 154(3) and by adding a historical note. These amended and added provisions read as follows:

§ 1.154 Statutory provisions; cross references.

SEC. 154. *Cross references.* * * *

(3) For exemptions of nonresident aliens, see section 873(b)(3).

* * * * *

[Sec. 154 as amended by sec. 103(c)(2), Foreign Investors Tax Act 1966 (80 Stat. 1551)]

PAR. 6. Section 1.337-5 is amended by revising paragraph (d) to read as follows:

§ 1.337-5 Special rules for certain minority shareholders.

* * * * *

(d) *Claim for credit or refund.* Claim for credit or refund of the tax deemed to have been paid by a shareholder pursuant to section 337(d) and paragraph (b) of this section shall be made on the shareholder's income tax return (or in an amended return or claim for credit or refund) for the taxable year in which he receives the first distribution in complete liquidation. In the case of a shareholder which is a partnership, claim shall be made by the partners for credit or refund of their distributive shares of the tax deemed to have been paid by the partnership. In the case of a shareholder which is an electing small business corporation (within the meaning of section 1371(b)), claim shall be made by those persons who are shareholders of such corporation on the last day of the corporation's taxable year in which it received the first distribution in complete liquidation. In the case of a shareholder which is exempt from tax under section 501(a) and to which section 511 does not apply for the taxable year, claim for refund of the tax deemed to have been paid by such shareholder shall be made on Form 843. For other rules applicable to the filing of claims for credit or refund of an overpayment of tax, see section 6402 and the regulations thereunder. For the limitations applicable to the credit or refund of an overpayment of tax, see section 6511 and the regulations thereunder.

* * * * *

PAR. 7. Section 1.852-9 is amended by revising paragraph (c) (2) (ii) to read as follows:

§ 1.852-9 Special procedural requirements applicable to designation under section 852(b) (3) (D).

* * * * *

(c) *Shareholders.* * * *

(2) *Credit or refund.* * * *

(ii) *Form to be used.* Claim for refund or credit of the tax deemed to have been paid by a shareholder with respect to an amount of undistributed capital gains shall be made on the shareholder's income tax return for the taxable year in which such amount of undistributed capital gains is includable in gross income. In the case of a shareholder which is a partnership, claim shall be made by the partners on their income tax returns for refund or credit of their distributive shares of the tax deemed to have been paid by the partnership. In the case of a shareholder which is exempt from tax under section 501(a) and to which section 511 does not apply for the taxable year, claim for refund of the tax deemed to have been paid by such shareholder on an amount of undistributed capital gains for such year shall be made on Form 843 and copy B of Form 2439 furnished to such shareholder shall be attached to its claim. For other rules applicable to the filing of claims for credit or refund of an overpayment of tax, see § 301.6402-2 of this chapter (Regulations on Procedure and Administration), relating to claims for credit or refund, and § 301.6402-3 of this chapter, relating to special rules applicable to income tax.

* * * * *

PAR. 8. Section 1.871 is amended by revising the heading thereof, by revising so much of section 871(a) as precedes paragraph (2) thereof, by revising section 871(b), and by revising the historical note, as follows:

§ 1.871A Statutory provisions; tax on nonresident alien individuals (before amendment by Foreign Investors Tax Act of 1966).

SEC. 871. *Tax on nonresident alien individuals*—(a) *No United States business—30 percent tax*—(1) *Imposition of tax.* Except as otherwise provided in subsection (b) there is hereby imposed for each taxable year, in lieu of the tax imposed by section 1, on the amount received, by every nonresident alien individual not engaged in trade or business within the United States, from sources within the United States, ~~as~~ interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income (including amounts described in section 402(a) (2), section 403(a) (2), section 631 (b) and (c), and section 1235, which are considered to be gains from the sale or exchange of capital assets), a tax of 30 percent of such amount.

* * * * *

(b) *No United States business—regular tax.* A nonresident alien individual not engaged in trade or business within the United States shall be taxable without regard to subsection (a) if during the taxable year the sum of the aggregate amount received from the sources specified in subsection (a) (1), plus the amount by which gains from sales or exchanges of capital assets exceed losses from such sales or exchanges (determined in accordance with subsection (a) (2)) is more than $19,000 in the case of a taxable year beginning in 1964 or more than $21,200 in the case of a taxable year beginning after 1964, except that—

(1) The gross income shall include only income from the sources specified in subsection (a) (1) plus any gain (to the extent provided in subchapter P; sec. 1201 and following, relating to capital gains and losses) from a sale or exchange of a capital asset if such gain would be taken into account were the tax being determined under subsection (a) (2);

(2) The deductions (other than the deduction for charitable contributions and gifts provided in section 873(c)) shall be allowed only if and to the extent that they are properly allocable to the gross income from the sources specified in subsection (a), except that any loss from the sale or exchange of a capital asset shall be allowed (to the extent provided in subchapter P without the benefit of the capital loss carryover provided in section 1212), if such loss would be taken into account were the tax being determined under subsection (a) (2).

If (without regard to this sentence) the amount of the taxes imposed in the base of such an individual under section 1 or under section 1201(b), minus the credit under section 35, is an amount which is less than 30 percent of the sum of—

(A) The aggregate amount received from the sources specified in subsection (a) (1), plus

(B) The amount, determined under subsection (a) (2), by which gains from sales or exchanges of capital assets exceed losses from such sales or exchanges,

then this subsection shall not apply and subsection (a) shall apply. For purposes of this subsection, the term "aggregate amount received from the sources specified in subsection (a) (1)" shall be applied without any exclusion under section 116.

* * * * *

[Sec. 871 as amended by secs. 40(a) and 41(a), Technical Amendments Act 1958 (72 Stat. 1638, 1639); sec. 2(b), Act of April 22, 1960 (Pub. L. 86-437, 74 Stat. 79); sec. 110(b), Mutual Educational and Cultural Exchange Act 1961 (75 Stat. 535); secs. 113(b) and 201(d) (12), Rev. Act 1964 (78 Stat. 24, 32); as in effect before amendment by sec. 103(a), Foreign Investors Tax Act 1966 (80 Stat. 1547)]

PAR. 9. Immediately before § 1.871-1 the following new section is inserted:

§ 1.871 Statutory provisions; tax on nonresident alien individuals (after amendment by Foreign Investors Tax Act of 1966).

SEC. 871. *Tax on nonresident alien individuals*—(a) *Income not connected with United States business—30 percent tax*—(1) *Income other than capital gains.* There is hereby imposed for each taxable year a tax of 30 percent of the amount received from sources within the United States by a nonresident alien individual as—

(A) Interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income,

(B) Gains described in section 402(a) (2), 403(a) (2), or 631 (b) or (c), and gains on transfers described in section 1235 made on or before October 4, 1966,

(C) In the case of bonds or other evidences of indebtedness issued after September 28, 1965, amounts which under section 1232 are considered as gains from the sale or exchange of property which is not a capital asset, and

(D) Gains from the sale or exchange after October 4, 1966, of patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, and other like property, or of any interest in any such property, to the extent such gains are from payments which are contingent on the productivity, use, or disposition of the property or interest sold or exchanged, or from payments which are treated as being so contingent under subsection (e), but only to the extent the amount so received is not effectively connected with the conduct of a trade or business within the United States.

(2) *Capital gains of aliens present in the United States 183 days or more.* In the case of a nonresident alien individual present in the United States for a period or periods aggregating 183 days or more during the taxable year, there is hereby imposed for such year a tax of 30 percent of the amount by which his gains, derived from sources within the United States, from the sale or exchange at any time during such year of capital assets exceed his losses, allocable to sources within the United States, from the sale or exchange at any time during such year of capital assets. For purposes of this paragraph, gains and losses shall be taken into account only if, and to the extent that, they would be recognized and taken into account if such gains and losses were effectively connected with the conduct of a trade or business within the United States, except that such gains and losses shall be determined without regard to section 1202 (relating to deduction for capital gains) and such losses shall be determined without the benefits of the capital loss carryover provided in section 1212. Any gain or loss which is taken into account in determining the tax under paragraph (1) or subsection (b) shall not be taken into account in determining the tax under this paragraph. For purposes of the 183-day requirement of this paragraph, a nonresident alien individual not engaged in trade or business within the United States who has not established a taxable year for any prior period shall be treated as having a taxable year which is the calendar year.

(b) *Income connected with United States business—graduated rate of tax*—(1) *Imposition of tax.* A nonresident alien individual engaged in trade or business within the United States during the taxable year shall be taxable as provided in section 1 or 1201(b) on his taxable income which is effectively connected with the conduct of a trade or business within the United States.

(2) *Determination of taxable income.* In determining taxable income for purposes of paragraph (1), gross income includes only gross income which is effectively connected with the conduct of a trade or business within the United States.

(c) *Participants in certain exchange or training programs.* For purposes of this section, a nonresident alien individual who (without regard to this subsection) is not engaged in trade or business within the United States and who is temporarily present in the United States as a nonimmigrant under subparagraph (F) or (J) of section

101(a)(15) of the Immigration and Nationality Act, as amended (8 U.S.C. 1101(a)(15) (F) or (J)), shall be treated as a nonresident alien individual engaged in trade or business within the United States, and any income described in section 1441(b) (1) or (2) which is received by such individual shall, to the extent derived from sources within the United States, be treated as effectively connected with the conduct of a trade or business within the United States.

(d) *Election to treat real property income as income connected with United States business*—(1) *In general*. A nonresident alien individual who during the taxable year derives any income—

(A) From real property held for the production of income and located in the United States, or from any interest in such real property, including (i) gains from the sale or exchange of such real property or an interest therein, (ii) rents or royalties from mines, wells, or other natural deposits, and (iii) gains described in section 631 (b) or (c), and

(B) Which, but for this subsection, would not be treated as income which is effectively connected with the conduct of a trade or business within the United States,

may elect for such taxable year to treat all such income as income which is effectively connected with the conduct of a trade or business within the United States. In such case, such income shall be taxable as provided in subsection (b)(1) whether or not such individual is engaged in trade or business within the United States during the taxable year. An election under this paragraph for any taxable year shall remain in effect for all subsequent taxable years, except that it may be revoked with the consent of the Secretary or his delegate with respect to any taxable year.

(2) *Election after revocation*. If an election has been made under paragraph (1) and such election has been revoked, a new election may not be made under such paragraph for any taxable year before the fifth taxable year which begins after the first taxable year for which such revocation is effective, unless the Secretary or his delegate consents to such new election.

(3) *Form and time of election and revocation*. An election under paragraph (1), and any revocation of such an election, may be made only in such manner and at such time as the Secretary or his delegate may by regulations prescribe.

(e) *Gains from sale or exchange of certain intangible property*. For purposes of subsection (a)(1)(D), and for purposes of sections 881(a)(4), 1441(b), and 1442(a)—

(1) *Payments treated as contingent on use, etc*. If more than 50 percent of the gain for any taxable year from the sale or exchange of any patent, copyright, secret process or formula, good will, trademark, trade brand, franchise, or other like property, or of any interest in any such property, is from payments which are contingent on the productivity, use, or disposition of such property or interest, all of the gain for the taxable year from the sale or exchange of such property or interest shall be treated as being from payments which are contingent on the productivity, use, or disposition of such property or interest.

(2) *Source rule*. In determining whether gains described in subsection (a)(1)(D) and section 881(a)(4) are received from sources within the United States, such gains shall be treated as rentals or royalties for the use of, or privilege of using, property or an interest in property.

(f) *Certain annuities received under qualified plans*. For purposes of this section, gross income does not include any amount received as an annuity under a qualified annuity plan described in section 403(a)(1), or from a qualified trust described in section 401(a) which is exempt from tax under section 501(a), if—

(1) All of the personal services by reason of which such annuity is payable were either (A) personal services performed outside the United States by an individual who, at the time of performance of such personal services, was a nonresident alien, or (B) personal services described in section 864(b)(1) performed within the United States by such individual, and

(2) At the time the first amount is paid as such annuity under such annuity plan, or by such trust, 90 percent or more of the employees for whom contributions or benefits are provided under such annuity plan, or under the plan or plans of which such trust is a part, are citizens or residents of the United States.

(g) *Cross references*. (1) For tax treatment of certain amounts distributed by the United States to nonresident alien individuals, see section 402(a)(4).

(2) For taxation of nonresident alien individuals who are expatriate U.S. citizens, see section 877.

(3) For doubling of tax on citizens of certain foreign countries, see section 891.

(4) For adjustment of tax in case of nationals or residents of certain foreign countries, see section 896.

(5) For withholding of tax at source on nonresident alien individuals, see section 1441.

(6) For the requirement of making a declaration of estimated tax by certain nonresident alien individuals, see section 6015(i).

[Sec. 871 as amended by secs. 40(a) and 41 (a), Technical Amendments Act 1958 (72 Stat. 1638, 1639); sec. 2(b), Act of April 22, 1960 (Public Law 86-437, 74 Stat. 79); sec. 110(b), Mutual Educational and Cultural Exchange Act 1961 (75 Stat. 535); secs. 113 (b) and 201(d)(12), Rev. Act 1964 (78 Stat. 24, 32); sec. 103(a), Foreign Investors Tax Act 1966 (80 Stat. 1547)]

PAR. 10. Section 1.871-1 is revised to read as follows:

§ 1.871-1 Classification and manner of taxing alien individuals.

(a) *Classes of aliens*. For purposes of the income tax, alien individuals are divided generally into two classes, namely, resident aliens and nonresident aliens. Resident alien individuals are, in general, taxable the same as citizens of the United States; that is, a resident alien is taxable on income derived from all sources, including sources without the United States. See § 1.1-1(b). Nonresident alien individuals are taxable only on certain income from sources within the United States and on the income described in section 864(c)(4) from sources without the United States which is effectively connected for the taxable year with the conduct of a trade or business in the United States.

(b) *Classes of nonresident aliens*—(1) *In general*. For purposes of the income tax, nonresident alien individuals are divided into the following three classes:

(i) Nonresident alien individuals who at no time during the taxable year are engaged in a trade or business in the United States,

(ii) Nonresident alien individuals who at any time during the taxable year are, or are deemed under § 1.871-9 to be, engaged in a trade or business in the United States, and

(iii) Nonresident alien individuals who are bona fide residents of Puerto Rico during the entire taxable year.

An individual described in subdivision (i) or (ii) of this subparagraph is subject to tax pursuant to the provisions of subpart A (section 871 and following), part II, subchapter N, chapter 1 of the Code, and the regulations thereunder. See §§ 1.871-7 and 1.871-8. The provisions of subpart A do not apply to individuals described in subdivision (iii) of this subparagraph, but such individuals, except as provided in section 933 with respect to Puerto Rican source income, are subject to the tax imposed by section 1 or section 1201(b). See § 1.876-1.

(2) *Treaty income*. If the gross income of a nonresident alien individual described in subparagraph (1) (i) or (ii) of this paragraph includes income on which the tax is limited by tax convention, see § 1.871-12.

(3) *Exclusions from gross income*. For rules relating to the exclusion of certain items from the gross income of a nonresident alien individual, including annuities excluded under section 871(f), see §§ 1.872-2 and 1.894-1.

(4) *Expatriation to avoid tax*. For special rules applicable in determining the tax of a nonresident alien individual who has lost U.S. citizenship with a principal purpose of avoiding certain taxes, see section 877.

(5) *Adjustment of tax of certain nonresident aliens*. For the application of pre-1967 income tax provisions to residents of a foreign country which imposes a more burdensome income tax than the United States, and for the adjustment of the income tax of a national or resident of a foreign country which imposes a discriminatory income tax on the income of citizens of the United States or domestic corporations, see section 896.

(6) *Citizens of certain U.S. possessions*. For rules for treating as nonresident alien individuals certain citizens of possessions of the United States who are not otherwise citizens of the United States, see section 932 and § 1.932-1.

(d) *Effective date*. This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-1 and 1.871-7(a) (Rev. as of Jan. 1, 1971).

PAR. 11. Section 1.871-6 is amended to read as follows:

§ 1.871-6 Duty of withholding agent to determine status of alien payee.

(a) *Proof of status required*. If income is paid to an alien individual without withholding the tax under chapter 3 of the Code, except insofar as the regulations thereunder permit exemption from withholding, then the withholding agent must be prepared to justify the failure to withhold.

(b) *Evidence of residence.* A withholding agent may rely upon the evidence of residence afforded by the fact that the alien individual has filed Form 1078 or an equivalent written statement. This statement or form shall be filed in the manner prescribed in § 11441.5.

(c) *Cross reference.* For definition of the term "withholding agent," see § 1.1465-1.

(d) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-6 (Rev. as of Jan. 1, 1971).

PAR. 12. Section 1.871-7 is deleted and the following new sections are inserted in lieu thereof:

§ 1.871-7 Taxation of nonresident alien individuals not engaged in U.S. business.

(a) *Imposition of tax.* (1) This section applies for purposes of determining the tax of a nonresident alien individual who at no time during the taxable year is engaged in trade or business in the United States. However, see also § 1.871-8 where such individual is a student or trainee deemed to be engaged in trade or business in the United States or where he has an election in effect for the taxable year in respect to real property income. Except as otherwise provided in § 1.871-12, a nonresident alien individual to whom this section applies is not subject to the tax imposed by section 1 or section 1201(b) but, pursuant to the provision of section 871(a), is liable to a flat tax of 30 percent upon the aggregate of the amounts determined under paragraphs (b), (c), and (d) of this section which are received during the taxable year from sources within the United States. Except as specifically provided in such paragraphs, such amounts do not include gains from the sale or exchange of property. To determine the source of such amounts, see sections 861 through 863, and the regulations thereunder.

(2) The tax of 30 percent is imposed by section 871(a) upon an amount only to the extent the amount constitutes gross income. Thus, for example, the amount of an annuity which is subject to such tax shall be determined in accordance with section 72.

(3) Deductions shall not be allowed in determining the amount subject to tax under this section except that losses from sales or exchanges of capital assets shall be allowed to the extent provided in section 871(a)(2) and paragraph (d) of this section.

(4) Except as provided in §§ 1.871-9 and 1.871-10, a nonresident alien individual not engaged in trade or business in the United States during the taxable year has no income, gain, or loss for the taxable year which is effectively connected for the taxable year with the conduct of a trade or business in the United States. See section 864(c)(1)(B) and § 1.864-3.

(5) Gains and losses which, by reason of section 871(d) and § 1.871-10, are treated as gains or losses which are effectively connected for the taxable year with the conduct of a trade or business in the United States by the nonresident alien individual shall not be taken into account in determining the tax under this section. See, for example, paragraph (c)(2) of §1.871-10.

(6) For special rules applicable in determining the tax of certain nonresident alien individuals, see paragraph (b) of § 1.871-1.

(b) *Fixed or determinable annual or periodical income.* The tax of 30 percent imposed by section 871(a)(1) applies to the gross amount received from sources within the United States as fixed or determinable annual or periodical gains, profits, or income. Specific items of fixed or determinable annual or periodical income are enumerated in section 871(a)(1)(A) as interest, dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, and emoluments, but other items of fixed or determinable annual or periodical gains, profits, or income are also subject to the tax, as, for instance, royalties, including royalties for the use of patents, copyrights, secret processes and formulas, and other like property. As to the determination of fixed or determinable annual or periodical income, see paragraph (a) of § 1.1441-2. For special rules treating gain on the disposition of section 306 stock as fixed or determinable annual or periodical income for purposes of section 871(a), see section 306(f) and paragraph (h) of § 1.306-3.

(c) *Other income and gains*—(1) *Items subject to tax.* The tax of 30 percent imposed by section 871(a)(1) also applies to the following gains received during the taxable year from sources within the United States:

(i) Gains described in section 402(a)(2), relating to the treatment of total distributions from certain employees' trusts; section 403(a)(2), relating to treatment of certain payments under certain employee annuity plans; and section 631 (b) or (c), relating to treatment of gain on the disposal of timber, coal, or iron ore with a retained economic interest;

(ii) [Reserved]

(iii) Gains on transfers described in section 1235, relating to certain transfers of patent rights, made on or before October 4, 1966; and

(iv) Gains from the sale or exchange after October 4, 1966, of patents, copyrights, secret processes and formulas, good will, trademarks, trade brands, franchises, or other like property, or of any interest in any such property, to the extent the gains are from payments (whether in a lump sum or in installments) which are contingent on the productivity, use or disposition of the property or interest sold or exchanged, or from payments which are treated under section 871(e) and § 1.871-11 as being so contingent.

(2) *Nonapplication of 183-day rule.* The provisions of section 871(a)(2), relating to gains from the sale or exchange of capital assets, and paragraph (d)(2) of this section do not apply to the gains described in this paragraph; as a consequence, the taxpayer receiving gains described in subparagraph (1) of this paragraph during a taxable year is subject to the tax of 30 percent thereon without regard to the 183-day rule contained in such provisions.

(3) *Determination of amount of gain.* The tax of 30 percent imposed upon the gains described in subparagraph (1) of this paragraph applies to the full amount of the gains and is determined (i) without regard to the alternative tax imposed by section 1201(b) upon the excess of the net long-term capital gain over the net short-term capital loss; (ii) without regard to the deduction allowed by section 1202 in respect of capital gains; (iii) without regard to section 1231, relating to property used in the trade or business and involuntary conversions; and (iv), except in the case of gains described in subparagraph (1)(ii) of this paragraph, whether or not the gains are considered to be gains from the sale or exchange of property which is a capital asset.

(d) *Gains from sale or exchange of capital assets*—(1) *Gains subject to tax.* The tax of 30 percent imposed by section 871(a)(2) applies to the excess of gains derived from sources within the United States over losses allocable to sources within the United States, which are derived from the sale or exchange of capital assets, determined in accordance with the provisions of subparagraphs (2) through (4) of this paragraph.

(2) *Presence in the United States 183 days or more.* (i) If the nonresident alien individual has been present in the United States for a period or periods aggregating 183 days or more during the taxable year, he is liable to a tax of 30 percent upon the amount by which his gains, derived from sources within the United States, from sales or exchanges of capital assets effected at any time during the year exceed his losses, allocable to sources within the United States, from sales or exchanges of capital assets effected at any time during that year. Gains and losses from sales or exchanges effected at any time during such taxable year are to be taken into account for this purpose even though the nonresident alien individual is not present in the United States at the time the sales or exchanges are effected. In addition, if the nonresident alien individual has been present in the United States for a period or periods aggregating 183 days or more during the taxable year, gains and losses for such taxable year from sales or exchanges of capital assets effected during a previous taxable year beginning after December 31, 1966, are to be taken into account, but only if he was also present in the United States during such previous taxable year for a period or periods aggregating 183 days or more.

(ii) If the nonresident alien individual has not been present in the United States during the taxable year, or if he has been present in the United States for a period or periods aggregating less than 183 days during the taxable year, gains and losses from sales or exchanges of capital assets effected during the year are not to be taken into account, except as required by paragraph (c) of this section, in determining the tax of such individual even though the sales or exchanges are effected during his presence in the United States. Moreover, gains and losses for such taxable year from sales or exchanges of capital assets effected during a previous taxable year beginning after December 31, 1966, are not to be taken into account, even though the nonresident alien individual was present in the United States during such previous year for a period or periods aggregating 183 days or more.

(iii) For purposes of this subparagraph, a nonresident alien individual is not considered to be present in the United States by reason of the presence in the United States of a person who is an agent or partner of such individual or who is a fiduciary of an estate or trust of which such individual is a beneficiary or a grantor-owner to whom section 671 applies.

(iv) The application of this subparagraph may be illustrated by the following examples:

Example (1) B, a nonresident alien individual not engaged in trade or business in the United States and using the calendar year as the taxable year, is present in the United States from May 1, 1971, to November 15, 1971, a period of more than 182 days. While present in the United States, B effects for his own account on various dates a number of transactions in stocks and securities on the stock exchange, as a result of which he has recognized capital gains of $10,000. During the period from January 1, 1971, to April 30, 1971, he carries out similar transactions through an agent in the United States, as a result of which B has recognized capital gains of $5,000. On December 15, 1971, through an agent in the United States B sells a capital asset on the installment plan, no payments being made by the purchaser in 1971. During 1972, B receives installment payments of $50,000 on the installment sale made in 1971, and the capital gain from sources within the United States for 1972 attributable to such payments is $12,500. In addition, during the period from January 1, 1972, to May 31, 1972, B effects for his own account, through an agent in the United States, a number of transactions in stocks and securities on the stock exchange, as a result of which B has recognized capital gains of $20,000. At no time during 1972 is B present in the United States or engaged in trade or business in the United States. Accordingly, for 1971, B is subject to tax under section 871(a)(2) on his capital gains of $15,000 from the transactions in that year on the stock exchange. For 1972, B is not subject to tax on the capital gain of $12,500 from the installment sale in 1971 or on the capital gains of $20,000 from the transactions in 1972 on the stock exchange.

Example (2). The facts are the same as in example (1) except that B is present in the United States from June 15, 1972, to December 31, 1972, a period of more than 182 days. Accordingly, B is subject to tax under section 871(a)(2) for 1971 on his capital gains of $15,000 from the transactions in that year on the stock exchange. He is also subject to tax under section 871(a)(2) for 1972 on his capital gains of $32,500 ($12,500 from the installment sale in 1971 plus $20,000 from the transactions in 1972 on the stock exchange).

Example (3). D, a nonresident alien individual not engaged in trade or business in the United States and using the calendar year as the taxable year, is present in the United States from April 1, 1971, to August 31, 1971, a period of less than 183 days. While present in the United States, D effects for his own account on various dates a number of transactions in stocks and securities on the stock exchange, as a result of which he has recognized capital gains of $15,000. During the period from January 1, 1971, to March 31, 1971, he carries out similar transactions through an agent in the United States, as a result of which D has recognized capital gains of $8,000. On December 20, 1971, through an agent in the United States D sells a capital asset on the installment plan, no payments being made by the purchaser in 1971. During 1972, D receives installment payments of $200,000 on the installment sale made in 1971, and the capital gain from sources within the United States for 1972 attributable to such payments is $50,000. In addition, during the period from Feburary 1, 1972, to August 15, 1972, a period of more than 182 days, D effects for his own account, through an agent in the United States, a number of transactions in stocks and securities on the stock exchange, as a result of which D has recognized capital gains of $25,000. At no time during 1972 is D present in the United States or engaged in trade or business in the United States. Accordingly, D is not subject to tax for 1971 or 1972 on any of his recognized capital gaiñs.

Example (4). The facts are the same as in example (3) except that D is present in the United States from February 1, 1972, to August 15, 1972, a period of more than 182 days. Accordingly, D is not subject to tax for 1971 on his capital gains of $23,000 from the transactions in that year on the stock exchange. For 1972 he is subject to tax under section 871(a)(2) on his capital gains of $25,000 from the transactions in that year on the stock exchange, but he is not subject to the tax on the capital gain of $50,000 from the installment sale in 1971.

(3) *Determination of 183-day period*—(i) *In general*. In determining the total period of presence in the United States for a taxable year for purposes of subparagraph (2) of this paragraph, all separate periods of presence in the United States during the taxable year are to be aggregated. If the nonresident alien individual has not previously established a taxable year, as defined in section 441(b), he shall be treated as having a taxable year which is the calendar year, as defined in section 441(d). Subsequent adoption by such individual of a fiscal year as the taxable year will be treated as a change in the taxpayer's annual accounting period to which section 442 applies, and the change must be authorized under this part (Income Tax Regulations) or prior approval must be obtained by filing an application on Form 1128 in accordance with paragraph (b) of § 1.442-1. If in the course of his taxable year the nonresident alien individual changes his status from that of a citizen or resident of the United States to that of a nonresident alien individual, or vice versa, the determination of whether the individual has been present in the United States for 183 days or more during the taxable year shall be made by taking into account the entire taxable year, and not just that part of the taxable year during which he has the status of a nonresident alien individual.

(ii) *Definition of "day"*. The term "day", as used in subparagraph (2) of this paragraph, means a calendar day during any portion of which the nonresident alien individual is physically present in the United States (within the meaning of sections 7701(a)(9) and 638) except that, in the case of an individual who is a resident of Canada or Mexico and, in the normal course of his employment in transportation service touching points within both Canada or Mexico and the United States, performs personal services in both the foreign country and the United States, the following rules shall apply:

(*a*) The performance of labor or personal services during 8 hours or more in any 1 day within the United States shall be considered as 1 day in the United States, except that if a period of more or less than 8 hours is considered a full workday in the transportation job involved, such period shall be considered as 1 day within the United States.

(*b*) The performance of labor or personal services during less than 8 hours in any day in the United States shall, except as provided in (*a*) of this subdivision, be considered as a fractional part of a day in the United States. The total number of hours during which such services are performed in the United States during the taxable year, when divided by eight, shall be the number of days during which such individual shall be considered present in the United States during the taxable year.

(*c*) The aggregate number of days determined under (*a*) and (*b*) of this subdivision shall be considered the total number of days during which such individual is present in the United States during the taxable year.

(4) *Determination of amount of excess gains*—(i) *In general*. For the purpose of determining the excess of gains over losses subject to tax under this paragraph, gains and losses shall be taken into account only if, and to the extent that, they would be recognized and taken into account if the nonresident alien individual were engaged in trade or business in the United States during the taxable year and such gains and losses were effectively connected for such year with the conduct of a trade or business in the United States by such individual. However, in determining such excess of gains over losses no deduction may be taken under section 1202, relating to the deduction for capital gains, or section 1212, relating to the capital loss carryover. Thus, for example, in determining such excess gains all amounts considered under chapter 1 of the Code as gains or losses from the sale or exchange of capital assets shall be taken into account, except those gains which are described in section 871(a)(1) (B) or (D) and taken into account under paragraph (c) of this section and are considered to be gains from the sale or exchange of capital assets. Also, for example, a loss described in section 631 (b) or (c) which is considered to be a loss from the sale of a

capital asset shall be taken into account in determining the excess gains which are subject to tax under this paragraph. In further illustration, in determining such excess gains no deduction shall be allowed, pursuant to the provisions of section 267, for losses from sales or exchanges of property between related taxpayers. Any gains which are taken into account under section 871(a)(1) and paragraph (c) of this section shall not be taken into account in applying section 1231 for purposes of this paragraph. Gains and losses are to be taken into account under this paragraph whether they are short-term or long-term capital gains or losses within the meaning of section 1222.

(ii) *Gains not included.* The provisions of this paragraph do not apply to any gains described in section 871(a)(1)(B) or (D), and in subdivision (i), (iii), or (iv) of paragraph (c)(1) of this section, which are considered to be gains from the sale or exchange of capital assets.

(iii) *Allowance of losses.* In determining the excess of gains over losses subject to tax under this paragraph losses shall be allowed only to the extent provided by section 165(c). Losses from sales or exchanges of capital assets in excess of gains from sales or exchanges of capital assets shall not be taken into account.

(e) *Credits against tax.* The credits allowed by section 31 (relating to tax withheld on wages), by section 32 (relating to tax withheld at source on nonresident aliens), by section 39 (relating to certain uses of gasoline and lubricating oil), and by section 6402 (relating to overpayments of tax) shall be allowed against the tax of a nonresident alien individual determined in accordance with this section.

(f) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-7 (b) and (c) (Rev. as of Jan. 1, 1971).

§ 1.871-8 Taxation of nonresident alien individuals engaged in U.S. business or treated as having effectively connected income.

(a) *Segregation of income.* This section applies for purposes of determining the tax of a nonresident alien individual who at any time during the taxable year is engaged in trade or business in the United States. It also applies for purposes of determining the tax of a nonresident alien student or trainee who is deemed under section 871(c) and § 1.871-9 to be engaged in trade or business in the United States or of a nonresident alien individual who at no time during the taxable year is engaged in trade or business in the United States but has an election in effect for the taxable year under section 871(d) and § 1.871-10 in respect to real property income. A nonresident alien individual to whom this section applies must segregate his gross income for the taxable year into two categories, namely (1) the income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, and (2) the income which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. A separate tax shall then be determined upon each such category of income, as provided in paragraph (b) of this section. The determination of whether income or gain is or is not effectively connected for the taxable year with the conduct of a trade or business in the United States by the nonresident alien individual shall be made in accordance with section 864(c) and §§ 1.864-3 through 1.864-7. For purposes of this section income which is effectively connected for the taxable year with the conduct of a trade or business in the United States includes all income which is treated under section 871 (c) or (d) and § 1.871-9 or § 1.871-10 as income which is effectively connected such year with the conduct of a trade or business in the United States by the nonresident alien individual.

(b) *Imposition of tax*—(1) *Income not effectively connected with the conduct of a trade or business in the United States.* If a nonresident alien individual who is engaged in trade or business in the United States at any time during the taxable year derives during such year from sources within the United States income or gains described in section 871 (a)(1), and paragraph (b) or (c) of § 1.871-7 or gains from the sale or exchange of capital assets determined as provided in section 871(a)(2) and paragraph (d) of § 1.871-7, which are not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, such income or gains shall be subject to a flat tax of 30 percent of the aggregate amount of such items. This tax shall be determined in the manner, and subject to the same conditions, set forth in § 1.871-7 as though the income or gains were derived by a nonresident alien individual not engaged in trade or business in the United States during the taxable year, except that (i) the rule in paragraph (d)(3) of such section for treating the calendar year as the taxable year shall not apply and (ii) in applying paragraph (c) and (d)(4) of such section, there shall not be taken into account any gains or losses which are taken into account in determining the tax under section 871(b) and subparagraph (2) of this paragraph. A nonresident alien individual who has an election in effect for the taxable year under section 871(d) and § 1.871-10 and who at no time during the taxable year is engaged in trade or business in the United States must determine his tax under § 1.871-7 on his income which is not treated as effectively connected with the conduct of a trade or business in the United States, subject to the exception contained in subdivision (ii) of this subparagraph.

(2) *Income effectively connected with the conduct of a trade or business in the United States*—(i) *In general.* If a nonresident alien to whom this section applies derives income or gains which are effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, the taxable income or gains shall, except as provided in § 1.871-12, be taxed in accordance with section 1 or, in the alternative, section 1201(b). See section 871(b)(1). Any income of the nonresident alien individual which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual shall not be taken into account in determining either the rate or amount of such tax. See paragraph (b) of § 1.872-1.

(ii) *Determination of taxable income.* The taxable income for any taxable year for purposes of this subparagraph consists only of the nonresident alien individual's taxable income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual; and, for this purpose, it is immaterial that the trade or business with which that income is effectively connected is not the same as the trade or business carried on in the United States by that individual during the taxable year. See example (2) in § 1.864-4(b). In determining such taxable income all amounts constituting, or considered to be, gains or losses for the taxable year from the sale or exchange of capital assets shall be taken into account if such gains or losses are effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, and, for such purpose, the 183-day rule set forth in section 871(a)(2) and paragraph (d)(2) of § 1.871-7 shall not apply. Losses which are not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual shall not be taken into account in determining taxable income under this subdivision, except as provided in section 873(b)(1).

(iii) *Cross references.* For rules for determining the gross income and deductions for the taxable year, see sections 872 and 873, and the regulations thereunder.

(c) *Change in trade or business status*—(1) *In general.* The determination as to whether a nonresident alien individual is engaged in trade or business within the United States during the taxable year is to be made for each taxable year. If at any time during the taxable year he is engaged in a trade or business in the United States, he is considered to be engaged in trade or business within the United States during the taxable year for purposes of sections 864(c)(1) and 871(b), and the regulations thereunder. Income, gain, or loss of a nonresident alien individual is not treated as being effectively connected for the taxable year with the conduct of a trade or business in the United States if he is not engaged in trade or business within the United States during such year, even though such income, gain, or loss may have been effectively connected for a previous taxable year with the conduct of a trade or business in the United

States. See § 1.864-3. However, income, gain, or loss which is treated as effectively connected for the taxable year with the conduct of a trade or business in the United States by a nonresident alien individual will generally be treated as effectively connected for a subsequent taxable year if he is engaged in a trade or business in the United States during such subsequent year, even though such income, gain, or loss is not effectively connected with the conduct of the trade or business carried on in the United States during such subsequent year. This subparagraph does not apply to income described in section 871 (c) or (d). It may not apply to a nonresident alien individual who for the taxable year uses an accrual method of accounting or to income which is constructively received in the taxable year within the meaning of § 1.451-2.

(2) *Illustrations.* The application of this paragraph may be illustrated by the following examples:

Example (1). B, a nonresident alien individual using the calendar year as the taxable year and the cash receipts and disbursements method of accounting, is engaged in business (business R) in the United States from January 1, 1971, to August 31, 1971. During the period of September 1, 1971, to December 31, 1971, B receives installment payments of $30,000 on sales made in the United States by business R during that year, and the income from sources within the United States for that year attributable to such payments is $7,509. On September 15, 1971, another business (business S), which is carried on by B only in a foreign country sells to U.S. customers on the installment plan several pieces of equipment from inventory. During the period of September 16, 1971, to December 31, 1971, B receives installment payments of $50,000 on these sales by business S, and the income from sources within the United States for that year attributable to such payments is $10,000. Under section 864(c)(3) and paragraph (b) of § 1.864-4 the entire income of $17,500 is effectively connected for 1971 with the conduct of a business in the United States by B. Accordingly, such income is taxable to B under paragraph (b)(2) of this section.

Example (2). Assume the same facts as in example (1), except that during 1972 B receives installment payments of $20,000 from the sales made during 1971 in the United States by business R, and of $80,000 from the sales made in 1971 to U.S. customers by business S, the total income from sources within the United States for 1972 attributable to such payments being $13,000. At no time during 1972 is B engaged in a trade or business in the United States. Under section 864(c)(1)(B) the income of $13,000 for 1972 is not effectively connected with the conduct of a trade or business in the United States by B. Moreover, such income is not fixed or determinable annual or periodical income. Accordingly, no amount of such income is taxable to B under section 871.

Example (3). Assume the same facts as in example (2), except that during 1972 B is engaged in a new business (business T) in the United States from July 1, 1972, to December 31, 1972. Under section 864(c)(3) and paragraph (b) of § 1.864-4, the income of $13,000 is effectively connected for 1972 with the conduct of a business in the United States by B. Accordingly, such income is taxable to B under paragraph (b)(2) of this section.

Example (4). Assume the same facts as in example (2), except that the installment payments of $20,000 from the sales made during 1971 in the United States by business R and not received by B until 1972 could have been received by B in 1971 if he had so desired. Under § 1.451-2, B is deemed to have constructively received the payments of $20,000 in 1971. Accordingly, the income attributable to such payments is effectively connected for 1971 with the conduct of a business in the United States by B and is taxable to B in 1971 under paragraph (b)(2) of this section.

(d) *Credits against tax.* The credits allowed by section 31 (relating to tax withheld on wages), section 32 (relating to tax withheld at source on nonresident aliens), section 33 (relating to the foreign tax credit), section 35 (relating to partially tax-exempt interest), section 38 (relating to investment in certain depreciable property), section 39 (relating to certain uses of gasoline and lubricating oil), section 40 (relating to expenses of work incentive programs), and section 6402 (relating to overpayments of tax) shall be allowed against the tax determined in accordance with this section. However, the credits allowed by sections 33, 38, and 40 shall not be allowed against the flat tax of 30 percent imposed by section 871(a) and paragraph (b)(1) of this section. Moreover, no credit shall be allowed under section 35 to a nonresident alien individual with respect to whom a tax is imposed for the taxable year under section 871(a) and paragraph (b)(1) of this section, even though such individual has income for such year upon which tax is imposed under section 871 (b) and paragraph (b)(2) of this section. For special rules applicable in determining the foreign tax credit, see section 906 (b) and the regulations thereunder. For the disallowance of certain credits where a return is not filed for the taxable year, see section 874 and § 1.874-1.

(e) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-7(d) (Rev. as of Jan. 1, 1971).

§ 1.871-9 Nonresident alien students or trainees deemed to be engaged in U.S. business.

(a) *Participants in certain exchange or training programs.* For purposes of §§ 1.871-7 and 1.871-8 a nonresident alien individual who is temporarily present in the United States during the taxable year as a nonimmigrant under subparagraph (F) (relating to the admission of students into the United States) or subparagraph (J) (relating to the admission of teachers, trainees, specialists, etc., into the United States) of section 101(a)(15) of the Immigration and Nationality Act (8 U.S.C. 1101(a)(15) (F) or (J)), and who without regard to this paragraph is not engaged in trade or business in the United States during such year, shall be deemed to be engaged in trade or business in the United States during the taxable year. For purposes of determining whether an alien who is present in the United States on an F visa or a J visa is a resident of the United States, see § 1.871-2.

(b) *Income treated as effectively connected with U.S. business.* Any income described in paragraph (1) (relating to the nonexcluded portion of certain scholarship or fellowship grants) or paragraph (2) (relating to certain nonexcluded expenses incident to such grants) of section 1441(b) which is received during the taxable year from sources within the United States by a nonresident alien individual described in paragraph (a) of this section is to be treated for purposes of §§ 1.871-7, 1.871-8, 1.872-1, and 1.873-1 as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. However, such income is not to be treated as effectively connected for the taxable year with the conduct of a trade or business in the United States for purposes of section 1441(c)(1) and paragraph (a) of § 1.1441-4. For exclusion relating to compensation paid to such individual by a foreign employer, see paragraph (b) of § 1.872-2.

(c) *Exchange visitors.* For purposes of paragraph (a) of this section a nonresident alien individual who is temporarily present in the United States during the taxable year as a nonimmigrant under subparagraph (J) of section 101(a)(15) of the Immigration and Nationality Act includes a nonresident alien individual admitted to the United States as an "exchange visitor" under section 201 of the U.S. Information and Educational Exchange Act of 1948 (22 U.S.C. 1446), which section was repealed by section 111 of the Mutual Educational and Cultural Exchange Act of 1961 (75 Stat. 538).

(d) *Mandatory application of rule.* The application of this section is mandatory and not subject to an election by the taxpayer.

(e) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-7(a)(3) (Rev. as of Jan. 1, 1971).

§ 1.871-10 Election to treat real property income as effectively connected with U.S. business.

(a) *When election may be made.* A nonresident alien individual or foreign corporation which during the taxable year derives any income from real property which is located in the United States and, in the case of a nonresident alien individual, held for the production of income, or derives income from any interest in any such property, may elect, pursuant to section 871(d) or 882(d) and this section, to treat all such income as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that taxpayer. The election may be made whether or not the taxpayer is engaged in trade or business in the United States during the taxable year for which the election is made or whether or not the taxpayer has income from real property which for the taxable year is effectively connected with the conduct of a trade or business in the United States, but it may be made only with respect to that income from sources within the United States which, without regard to this section, is not effectively connected for the taxable year with the conduct of a trade or business in the United States by the taxpayer. If for the taxable year the taxpayer has no income from real property located in the United States, or from any interest in such property, which is subject to the tax imposed by section 871(a) or 881(a), the election may not be made. But if an election has been properly made under this section for a taxable year, the election remains in effect, unless properly revoked, for subsequent taxable years even though during any such subsequent taxable year there is no income from the real property, or interest therein, in respect of which the election applies.

(b) *Income to which the election applies*—(1) *Included income*. An election under this section shall apply to all income from real property which is located in the United States and, in the case of a nonresident alien individual, held for the production of income, and to all income derived from any interest in such property, including (i) gains from the sale or exchange of such property or an interest therein, (ii) rents or royalties from mines, oil or gas wells, or other natural resources, and (iii) gains described in section 631 (b) or (c), relating to treatment of gain on the disposal of timber, coal, or iron ore with a retained economic interest. The election may not be made with respect to only one class of such income. For purposes of the election, income from real property, or from any interest in real property, includes any amount included under section 652 or 662 in the gross income of a nonresident alien individual or foreign corporation that is the beneficiary of an estate or trust if, by reason of the application of section 652(b) or 662(b), and the regulations thereunder, such amount has the character in the hands of that beneficiary of income from real property, or from any interest in real property. It is immaterial that no tax would be imposed on the income by section 871(a) and paragraph (a) of § 1.871-7, or by section 881(a) and paragraph (a) of § 1.881-2, if the election were not in effect. Thus, for example, if an election under this section has been made by a nonresident alien individual not engaged in trade or business in the United States during the taxable year, the tax imposed by section 871(b)(1) and paragraph (b)(2) of § 1.871-8 applies to his gains derived from the sale of real property located in the United States and held for the production of income, even though such income would not be subject to tax under section 871(a) if the election had not been made. In further illustration, assume that a nonresident alien individual not engaged in trade or business, or present, in the United States during the taxable year has income from sources within the United States consisting of oil royalties, rentals from a former personal residence, and capital gain from the sale of another residence held for the production of income. If he makes an election under this section, it will apply with respect to his royalties, rentals, and capital gain, even though such capital gain would not be subject to tax under section 871(a) if the election had not been made.

(2) *Income not included*. For purposes of subparagraph (1) of this paragraph, income from real property, or from any interest in real property, does not include (i) interest on a debt obligation secured by a mortgage of real property, (ii) any portion of a dividend, within the meaning of section 316, which is paid by a corporation or a trust, such as a real estate investment trust described in section 857, which derives income from real property, (iii) in the case of a nonresident alien individual, income from real property, such as a personal residence, which is not held for the production of income or from any transaction in such property which was not entered into for profit, (iv) rentals from personal property, or royalties from intangible personal property, within the meaning of subparagraph (3) of this paragraph, or (v) income which, without regard to section 871(d) or 882(d) and this section, is treated as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States.

(3) *Rules applicable to personal property*. For purposes of subparagraph (2) of this paragraph, in the case of a sales agreement, or rental or royalty agreement, affecting both real and personal property, the income from the transaction is to be allocated between the real property and the personal property in proportion to their respective fair market values unless the agreement specifically provides otherwise. In the case of such a rental or royalty agreement, the respective fair market values are to be determined as of the time the agreement is signed. In making determinations of this subparagraph, the principles of paragraph (c) of § 1.48-1, relating to the definition of "section 38 property," apply for purposes of determining whether property is tangible or intangible personal property and of paragraph (a)(5) of § 1.1245-1 apply for purposes of making the allocation of income between real and personal property.

(c) *Effect of the election*—(1) *Determination of tax*. The income to which, in accordance with paragraph (b) of this section, an election under this section applies shall be subject to tax in the manner, and subject to the same conditions, provided by section 871(b)(1) and paragraph (b)(2) of § 1.871-8, or by section 882(a)(1) and paragraph (b)(2) of § 1.882-1. For purposes of determining such tax for the taxable year, income to which the election applies shall be aggregated with all other income of the nonresident alien individual or foreign corporation which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that taxpayer. To the extent that deductions are connected with income from real property to which the election applies, they shall be treated for purposes of section 873(a) or section 882(c)(1) as connected with income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by the nonresident alien individual or foreign corporation. An election under this section does not cause a nonresident alien individual or foreign corporation, which is not engaged in trade or business in the United States during the taxable year, to be treated as though such taxpayer were engaged in trade or business in the United States during the taxable year. Thus, for example, the compensation received during the taxable year for services performed in the United States in a previous taxable year by a nonresident alien individual, who has an election in effect for the taxable year under this section but is engaged in trade or business in the United States at no time during the taxable year, is not effectively connected for the taxable year with the conduct of a trade or business in the United States. In further illustration, gain for the taxable year from the casual sale of personal property described in section 1221 (I) derived by a nonresident alien individual who is not engaged in trade or business in the United States during the taxable year but has an election in effect for such year under this section is not effectively connected with the conduct of a trade or business in the United States. See § 1.864-3. If an election under this section is in effect for the taxable year, the income to which the election applies shall be treated, for purposes of section 871(b)(1) or section 882(a)(1), section 1441(c)(1), and paragraph (a) of § 1.1441-4, as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by the taxpayer.

(2) *Treatment of property to which election applies*. Any real property, or interest in real property, with respect to which an election under this section applies shall be treated as a capital asset which, if depreciable, is subject to the allowance for depreciation provided in section 167 and the regulations thereunder. Such property, or interest in property, shall be treated as property not used in a trade or business for purposes of applying any provisions of the Code, such as section 172(d)(4)(A), relating to gain or loss attributable to a trade or business for purposes of determining a net operating loss; section 1221(2), relating to property not constituting a capital asset; or section 1231(b), relating to special rules for treatment of gains and losses. For example, if a nonresident alien individual makes the election under this section and, while the election is in effect, sells unimproved land which is located in the United States and held for investment

purposes, any gain or loss from the sale shall be considered gain or loss from the sale of a capital asset and shall be treated, for purposes of determining the tax under section 871(b)(1) and paragraph (b)(2) of § 1.871–8, as a gain or loss which is effectively connected for the taxable year with the conduct of a trade or business in the United States.

(d) *Manner of making or revoking an election*—(1) *Election, or revocation, without consent of Commissioner*—(i) *In general.* A nonresident alien individual or foreign corporation may, for the first taxable year for which the election under this section is to apply, make the initial election at any time before the expiration of the period prescribed by section 6511(a), or by section 6511(c) if the period for assessment is extended by agreement, for filing a claim for credit or refund of the tax imposed by chapter 1 of the Code for such taxable year. This election may be made without the consent of the Commissioner. Having made the initial election, the taxpayer may, within the time prescribed for making the election for such taxable year, revoke the election without the consent of the Commissioner. If the revocation is timely and properly made, the taxpayer may make his initial election under this section for a later taxable year without the consent of the Commissioner. If the taxpayer revokes the initial election without the consent of the Commissioner he must file amended income tax returns, or claims for credit or refund, where applicable, for the taxable years to which the revocation applies.

(ii) *Statement to be filed with return.* An election made under this section without the consent of the Commissioner shall be made for a taxable year by filing with the income tax return required under section 6012 and the regulations thereunder for such taxable year a statement to the effect that the election is being made. This statement shall include (*a*) a complete schedule of all real property, or any interest in real property, of which the taxpayer is titular or beneficial owner, which is located in the United States, (*b*) an indication of the extent to which the taxpayer has direct or beneficial ownership in each such item of real property, or interest in real property, (*c*) the location of the real property or interest therein, (*d*) a description of any substantial improvements on any such property, and (*e*) an identification of any taxable year or years in respect of which a revocation or new election under this section has previously occurred. This statement may not be filed with any return under section 6851 and the regulations thereunder.

(iii) *Exemption from withholding of tax.* For statement to be filed with a withholding agent at the beginning of a taxable year in respect of which an election under this section is to be made, see paragraph (a) of § 1.1441–4.

(2) *Revocation, or election, with consent of Commissioner*—(i) *In general.* If the nonresident alien individual or foreign corporation makes the initial election under this section for any taxable year and the period prescribed by subparagraph (1)(i) of this paragraph for making the election for such taxable year has expired, the election shall remain in effect for all subsequent taxable years, including taxable years for which the taxpayer realizes no income from real property, or from any interest therein, or for which he is not required under section 6012 and the regulations thereunder to file an income tax return. However, the election may be revoked in accordance with subdivision (iii) of this subparagraph for any subsequent taxable year with the consent of the Commissioner. If the election for any such taxable year is revoked with the consent of the Commissioner, the taxpayer may not make a new election before his fifth taxable year which begins after the first taxable year for which the revocation is effective unless consent is given to such new election by the Commissioner in accordance with subdivision (iii) of this subparagraph.

(ii) *Effect of new election.* A new election made for the fifth taxable year, or taxable year thereafter, without the consent of the Commissioner, and a new election made with the consent of the Commissioner, shall be treated as an initial election to which subparagraph (1) of this paragraph applies.

(iii) *Written request required.* A request to revoke an election made under this section when such revocation requires the consent of the Commissioner, or to make a new election when such election requires the consent of the Commissioner, shall be made in writing and shall be addressed to the Director of International Operations, Internal Revenue Service, Washington, D.C. 20225. The request shall include the name and address of the taxpayer and shall be signed by the taxpayer or his duly authorized representative. It must specify the taxable year for which the revocation or new election is to be effective and shall be filed within 75 days after the close of the first taxable year for which it is desired to make the change. The request must specify the grounds which are considered to justify the revocation or new election. The Director of International Operations may require such other information as may be necessary in order to determine whether the proposed change will be permitted. A copy of the consent by the Director of International Operations shall be attached to the taxpayer's return required under section 6012 and the regulations thereunder for the taxable year for which the revocation or new election is effective. A copy of such consent may not be filed with any return under section 6851 and the regulations thereunder.

(3) *Election by partnership.* If a nonresident alien individual or foreign corporation is a member of a partnership which has income described in paragraph (b)(1) of this section from real property, any election to be made under this section in respect of such income shall be made by the partners and not by the partnership.

(e) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. There are no corresponding rules in this part for taxable years beginning before January 1, 1967.

§ 1.871–11 Gains from sale or exchange of patents, copyrights, or similar property.

(a) *Contingent payment defined.* For purposes of section 871(a)(1)(D), section 881(a)(4), § 1.871–7(c)(1)(iv), § 1.881–2(c)(1)(iii), and this section, payments which are contingent on the productivity, use, or disposition of property or of an interest therein include continuing payments measured by a percentage of the selling price of the products marketed, or based on the number of units manufactured or sold, or based in a similar manner upon production, sale or use, or disposition of the property or interest transferred. A payment which is certain as to the amount to be received, but contingent as to the time of payment, or an installment payment of a principal sum agreed upon in a transfer agreement, shall not be treated as a contingent payment for purposes of this paragraph. For the inapplication of section 1253 to certain amounts described in this paragraph, see paragraph (a) of § 1.1253–1.

(b) *Payments treated as contingent on use.* Pursuant to section 871(e), if more than 50 percent of the gain of a nonresident alien individual or foreign corporation for any taxable year from the sale or exchange after October 4, 1966, of any patent, copyright, secret process or formula, goodwill, trademark, trade brand, franchise, or other like property, or of any interest in any such property, is from payments which are contingent on the productivity, use, or disposition of such property or interest, all of the gain of such individual or corporation for the taxable year from the sale or exchange of such property or interest are, for purposes of section 871(a)(1)(D), section 881(a)(4), section 1441(b), or section 1442(a), and the regulations thereunder, to be treated as being from payments which are contingent on the productivity, use, or disposition of such property or interest. This paragraph does not apply for purposes of determining under section 871(b)(1) or 882(a)(1) the tax of a nonresident alien individual or foreign corporation on income which is effectively connected for the taxable year with the conduct of a trade or business in the United States.

(c) *Sale or exchange.* A sale or exchange for purposes of this section includes, but is not limited to, a transfer by an individual which by reason of section 1235, relating to the sale or exchange of patents, is considered the sale or exchange of a capital asset. The provisions of section 1253, relating to transfers of franchises, trademarks, and trade names, do not apply in determining whether a transfer is a sale or exchange for purposes of this section.

(d) *Recovery of adjusted basis.* For purposes of determining for any taxable year the amount of gains which are subject to tax under section 871(a)(1)(D) or 881(a)(4), payments received by the nonresident alien individual or foreign corporation during such year must be reduced by amounts representing recovery of the taxpayer's adjusted basis of the property or interest which is sold or exchanged. Where the taxpayer receives in the same taxable year payments which, without reference to section 871(e) and this section, are not contingent on the productivity, use, or disposition of the property or interest which is sold or exchanged and payments which are contingent on the productivity, use, or disposition of the property or interest which is sold or exchanged, the taxpayer's unrecovered adjusted basis in the property or interest which is sold or exchanged must be allocated for the taxable year between such payments on the basis of the gross amount of each such type of payments. Where the taxpayer receives in the taxable year only payments which are not so contingent or only payments which are so contingent, the taxpayer's unrecovered basis must be allocated in its entirety to such payments for the taxable year.

(e) *Source rule.* In determining whether gains described in section 871(a)(1)(D) or 881(a)(4) and paragraph (b) of this section are received from sources within the United States, such gains shall be treated, for purposes of section 871(a)(1)(D), section 881(a)(4), section 1441(b), and section 1442(a), as rentals or royalties for the use of, or privilege of using, property or an interest in property. See section 861(a)(4), § 1.861-5, and paragraph (a) of § 1.862-1.

(f) *Illustrations.* The application of this section may be illustrated by the following examples:

Example (1). (a) A, a nonresident alien individual who uses the cash receipts and disbursements method of accounting and the calendar year as the taxable year, holds a U.S. patent which he developed through his own effort. On December 15, 1967, A enters into an agreement of sale with M Corporation, a domestic corporation, whereby A assigns to M Corporation all of his U.S. rights in the patent. In consideration of the sale, M Corporation is obligated to pay a fixed sum of $60,000, $20,000 being payable on execution of the contract and the balance payable in four annual installments of $10,000 each. As additional consideration, M Corporation agrees to pay to A a royalty in the amount of 2 percent of the gross sales of the products manufactured by M Corporation under the patent. A is not engaged in trade or business in the United States at any time during 1967 and 1968. His adjusted basis in the patent at the time of sale is $28,800.

(b) In 1967, A receives only the $20,000 paid by M Corporation on the execution of the contrac asot elf
the contract of sale. No gain is realized by A upon receipt of this amount, and his unrecovered adjusted basis in the patent is reduced to $8,800 ($28,800 less $20,000).

(c) In 1968, M Corporation has gross sales of $600,000 from products manufactured under the patent. Consequently, for 1968, M Corporation pays $22,000 to A, $10,000 being the annual installment on the fixed payment and $12,000 being payments under the terms of the royalty provision. A's recognized gain for 1968 is $13,200 ($22,000 reduced by the unrecovered adjusted basis of $8,800). Of the total gain of $13,200, gain in the amount of $6,000 ($10,000 - [$8,800 × $10,000/$22,000]) is considered to be from the fixed installment payment and of $7,200 ($12,000 - [$8,800 × $12,000/$22,000]) is considered to be from the royalty payment. Since 54.5 percent ($7,200/$13,200) of the gain recognized in 1968 from the sale of the patent is from payments which are contingent on the productivity, use, or disposition of the patent, all of the $13,200 gain recognized in 1968 is treated, for purposes of section 871(a)(1)(D) and section 1441(b), as being from payments which are contingent on the productivity, use, or disposition of the patent.

Example (2). (a) F, a foreign corporation using the calendar year as the taxable year and not engaged in trade or business in the United States, holds a U.S. patent on certain property which it developed through its own efforts. Corporation F uses the cash receipts and disbursements method of accounting. On December 1, 1966, F Corporation enters into an agreement of sale with D Corporation, a domestic corporation, whereby D Corporation purchases the exclusive right and license, and the right to sublicense to others, to manufacture, use, and/or sell certain devices under the patent in the United States during the term of the patent. The agreement grants D Corporation the right to dispose, anywhere in the world, of machinery manufactured in the United States and equipped with such devices. Corporation D is granted the right, at its own expense, to prosecute infringers in its own name or in the name of F Corporation, or both, and to retain any damages recovered.

(b) Corporation D agrees to pay to F Corporation annually $5 for each device manufactured under the patent during the year but in no case less than $5,000 per year. In 1967, D Corporation manufactures 2,500 devices under the patent; and, in 1968, 1,500 devices. Under the terms of the contract D Corporation pays to F Corporation in 1967 $12,500 with respect to production in that year and $7,500 in 1968 with respect to production in that year. F Corporation's basis in the patent at the time of the sale is $17,000.

(c) With respect to the payments received by F Corporation in 1967, no gain is realized by that corporation and its unrecovered adjusted basis in the patent is reduced to $4,500 ($17,000 less $12,500).

(d) With respect to the payments received by F Corporation in 1968, such corporation has recognized gain of $3,000 ($7,500 reduced by unrecovered adjusted basis of $4,500). Of the total gain of $3,000, gain in the amount of $2,000 ($5,000 - [$4,500 × $5,000/$7,500]) is considered to be from the fixed installment payment and of $1,000 ($2,500 - [$4,500 × $2,500/$7,500]) is considered to be from payments which are contingent on the productivity, use, or disposition of the patent. Since 33.3 percent ($1,000/$3,000) of the gain recognized in 1968 from the sale of the patent is from payments which are contingent on the productivity, use, or disposition of the patent, only $1,000 of the $3,000 gain for that year constitutes gains which, for purposes of section 881(a)(4) and section 1442(a), are from payments which are contingent on the productivity, use, or disposition of the patent. The balance of $2,000 is gain from the sale of property and is not subject to tax under section 881(a).

(g) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966, but only in respect of gains from sales or exchanges occurring after October 4, 1966. There are no corresponding rules in this part for taxable years beginning before January 1, 1967.

§ 1.871-12 Determination of tax on treaty income.

(a) *In general.* This section applies for purposes of determining under § 1.871-7 or § 1.871-8 the tax of a nonresident alien individual, or under § 1.881-2 or § 1.882-1 the tax of a foreign corporation, which for the taxable year has income described in section 872(a) or 882(b) upon which the tax is limited by an income tax convention to which the United States is a party. Income for such purposes does not include income of any kind which is exempt from tax under the provisions of an income tax convention to which the United States is a party. See §§ 1.872-2(c) and 1.883-1(b). This section shall not apply to a nonresident alien individual who is a bona fiide resident of Puerto Rico during the entire taxable year.

(b) *Definition of treaty and nontreaty income*—(1) *In general.* (i) For purposes of this section the term "treaty income" shall be construed to mean the gross income of a nonresident alien individual or foreign corporation, as the case may be, the tax on which is limited by a tax convention. The term "nontreaty income" shall be construed, for such purposes, to mean the gross income of the nonresident alien individual or foreign corporation other than the treaty income. Neither term includes income of any kind which is exempt from the tax imposed by chapter 1 of the Code.

(ii) In determining either the treaty or nontreaty income the gross income shall be determined in accordance with §§ 1.872-1 and 1.872-2, or with §§ 1.882-3 and 1.883-1, except that in determining the treaty income the exclusion granted by section 116(a) for dividends shall not be taken into account. Thus, for example, treaty income includes the total amount of dividends paid by a domestic corporation not disqualified by section 116(b) and received from sources within the United States if, in accordance with a tax convention, the dividends are subject to the income tax at a rate not to exceed 15 percent but does not include interest which, in accordance with a tax convention, is exempt from the income tax. In further illustration, neither the treaty nor the nontreaty income includes interest on certain governmental obligations which by reason of section 103 is excluded from gross income, or interest which by reason of a tax convention is exempt from the tax imposed by chapter 1 of the Code.

(iii) For purposes of applying any income tax convention to which the United States is a party, original issue discount which is subject to tax under section 871(a)(1)(C) or 881(a)(3) is to be treated as interest, and gains which are subject to tax under section 871(a)(1)(D) or 881(a)(4) are to be treated as royalty income. This subdivision shall not apply, however, where its application would be contrary to any treaty obligation of the United States.

(2) *Application of permanent establishment rule of treaties.* In applying this section with respect to income which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by a nonresident alien individual or foreign corporation, see section 894(b), which provides that with respect to such income the nonresident alien individual or foreign corporation shall be deemed not to have a permanent establishment in the United States at any time during the taxable year for purposes of applying any exemption from, or reduction in rate of, tax provided by any tax convention.

(c) *Determination of tax*—(1) *In general.* If the gross income of a nonresident alien individual or foreign corporation, as the case may be, consists of both treaty and nontreaty income, the tax liability for the taxable year shall be the sum of the amounts determined in accordance with subparagraphs (2) and (3) of this paragraph. In no case, however, may the tax liability so determined exceed the tax liability (tax reduced by allowable credits) with respect to the taxpayer's entire income, determined in accordance with § 1.871-7 or § 1.871-8, or with § 1.881-2 or § 1.882-1, as though the tax convention had not come into effect and without reference to the provisions of this section. Determinations under this paragraph shall be made without taking into account any credits allowed by sections 31, 32, 39, and 6402, but such credits shall be allowed against the tax liability determined in accordance with this subparagraph.

(2) *Tax on nontreaty income.* For purposes of subparagraph (1) of this paragraph, compute a partial tax (determined without the allowance of any credit) upon only the nontreaty income in accordance with § 187-1 or § 1.871-8, or with § 1.881-2 or § 1.882-1, whichever applies, as though the tax convention had not come into effect. To the extent allowed by paragraph (d) of § 1.871-8, or paragraph (c) of § 1.882-1, the credits allowed by sections 33, 35, 38, and 40 shall then be allowed, without taking into account any item included in the treaty income, against the tax determined under this subparagraph.

(3) *Tax on treaty income.* For purposes of subparagraph (1) of this paragraph, compute a tax upon the gross amount, determined without the allowance of any deduction, of each separate item of treaty income at the reduced rate applicable to that item under the tax convention. No credits shall be allowed against the tax determined under this subparagraph.

(d) *Illustrations.* The application of this section may be illustrated by the following examples:

Example (1). (a) A nonresident alien individual who is a resident of a foreign country with which the United States has entered into a tax convention receives during the taxable year 1967 from sources within the United States total gross income of $4,100, consisting of the following items and determined without regard to the $100 exclusion granted by section 116(a):

Dividends the tax on which is limited by the tax convention to a rate not to exceed 15 percent	$3,100
Compensation for personal services, the tax on which is not limited by the tax convention	1,000
Total gross income	4,100

(b) The dividends are paid by a domestic corporation not disqualified by section 116 (b). The taxpayer is engaged in business in the United States during the taxable year by reason of performing personal services in the United States for a period in excess of 90 days, but does not have a permanent establishment therein. Under paragraph (c) (6) (i) of § 1.864-4, the dividends are effectively connected for the taxable year with the conduct of a trade or business in the United States. Interest expense in the amount of $2,100 connected with the dividend income is paid by the taxpayer during the taxable year.

(c) The tax liability for the taxable year is $193, determined as follows:

Total gross income, determined by taking into account the exclusion granted by section 116(a)		$4,000
Less: Deduction for interest expense paid	$2,100	
Deduction for personal exemption	600	2,700
Taxable income		1,300
Tax under section 1 of the Code (determined as provided in § 1.871-8 (b) (2) as though the tax convention had not come into effect) ($145 plus 16 percent of $300)		193

(d) If the tax had been determined as provided in paragraph (c) (2) and (3) of this section, the tax liability would have been $521, determined as follows:

Nontreaty gross income	$1,000
Less: Deduction for personal exemption	600
Nontreaty taxable income	400
Tax under section 1 of the Code on nontreaty taxable income (14% of $400)	56
Plus: Tax on treaty income (gross dividends) ($3,100 × 15 percent)	465
Total tax	521

Example (2). (a) A nonresident alien individual who is a resident of a foreign country with which the United States has entered into a tax convention receives during the taxable year 1967 from sources within the United States total gross income of $22,000, consisting of the following items:

Compensation for personal services the tax on which is not limited by the tax convention (effectively connected income under § 1.864-4(c) (6) (ii))	$20,000
Oil royalties the tax on which is limited by the tax convention to 15 percent of the gross amount thereof (effectively connected income by reason of election under § 1.871-10)	2,000
Total gross income	22,000

(b) The taxpayer is engaged in business in the United States during the taxable year but does not have a permanent establishment therein. There are no allowable deductions, other than the deductions allowed by sections 613 and 873(b) (3).

(c) The tax liability for the taxable year is $6,100, determined as follows:

Nontreaty gross income	$20,000
Less: Deduction for personal exemption	600
Nontreaty taxable income	19,400
Tax under section 1 of the Code on nontreaty taxable income ($5,170 plus 45 percent of $1,400)	5,800
Plus: Tax on treaty income (Gross oil royalties) ($2,000 × 15 percent)	300
Total tax (determined as provided in paragraph (c) (2) and (3) of this section)	6,100

(d) If the tax had been determined under paragraph (b) (2) of § 1.871-8 as though the tax liability would have been $6,478, determ-
tax liability would have been $6,478, determined as follows and by taking into account the election under § 1.871-10:

Total gross income		$22,000
Less: Deduction under section 613 for percentage depletion ($2000 × 27½ percent)	$550	
Deduction for personal exemption	600	1,150
Taxable income		20,850
Tax under section 1 of the Code on taxable income ($6,070 plus 48 percent of $850)		6,478

(e) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.871-7(e) (Rev. as of Jan. 1, 1971).

§ 1.871-13 Taxation of individuals for taxable year of change of U.S. citizenship or residence.

(a) *In general.* (1) An individual who is a citizen or resident of the United States at the beginning of the taxable year but a nonresident alien at the end of the taxable year, or a nonresident alien at the beginning of the taxable year but a citizen or resident of the United States at the end of the taxable year, is taxable for such year as though his taxable year were comprised of two separate periods, one consisting of the time during which he is a citizen or resident of the United States and the other consisting of the time during which he is not a citizen or resident of the United States. Thus, for example, the income tax liability of an alien individual under chapter 1 of the Code for the taxable year in which he changes his residence will be computed under two different sets of rules, one relating to resident aliens for the period of residence and the other relating to nonresident aliens for the period of nonresidence. However, in determining the taxable income for such year which is subject to the graduated rate of tax imposed by section 1 or 1201 of the Code, all income for the period of U.S. citizenship or residence must be aggregated with the income for the period of nonresidence which is effectively connected for such year with the conduct of a trade or business in the United States.

(2) For purposes of this section, an individual is deemed to be a citizen or resident of the United States for the day on which he becomes a citizen or resident of the United States, a nonresident of the United States for the day on which he abandons his U.S. residence, and an alien for the day on which he gives up his U.S. citizenship.

(b) *Acquisition of U.S. citizenship or residence.* Income from sources without the United States which is not effectively connected with the conduct by the taxpayer of a trade or business in the United States is not taxable if received by an alien individual while he is not a resident of the United States even though he becomes a citizen or resident of the United States after its receipt and before the close of the taxable year. However, income from sources without the United States which is not effectively connected with the conduct by the taxpayer of a trade or business in the United States is taxable if received by an individual while he is a citizen or resident of the United States, even though he earns the income earlier in the taxable year while he is neither a citizen nor resident of the United States.

(c) *Abandonment of U.S. citizenship or residence.* Income from sources without the United States which is not effectively connected with the conduct by the taxpayer of a trade or business in the United States is not taxable if received by an alien individual while he is not a resident of the United States, even though he earns the income earlier in the taxable year while he is a citizen or resident of the United States. However, income from sources without the United States which is not effectively connected with the conduct by the taxpayer of a trade or business in the United States is taxable if received by an individual while he is a citizen or resident of the United States, even though he abandons his U.S. citizenship or residence after its receipt and before the close of the taxable year.

(d) *Special rules*—(1) *Method of accounting.* Paragraphs (b) and (c) of this section may not apply to an individual who for the taxable year uses an accrual method of accounting.

(2) *Deductions for personal exemptions.* An alien individual to whom this section applies is entitled to deduct one personal exemption for the taxable year under section 151. In addition, he is entitled to such additional exemptions as are allowed as a deduction under section 151 but only to the extent the amount of such additional exemptions do not exceed his taxable income (determined without regard to any deduction for personal exemptions) for the period in the taxable year during which he is a citizen or resident of the United States. This subparagraph does not apply to the extent it is inconsistent with section 873, and the regulations thereunder, or with the provisions of an income tax convention to which the United States is a party.

(3) *Exclusion of dividends received.* In determining the $100 exclusion for the taxable year provided by section 116 in respect of certain dividends, only those dividends for the period during which the individual is neither a citizen nor resident of the United States may be taken into account as are effectively connected for the taxable year with the conduct of a trade or business in the United States. See § 1.116–1(e)(1).

(e) *Illustrations.* The application of this section may be illustrated by the following examples:

Example (1). A, a married alien individual who uses the calendar year as the taxable year and the cash receipts and disbursements method of accounting, becomes a resident of the United States on June 1, 1971. During the period of nonresidence from January 1, 1971, to May 31, 1971, inclusive, A receives $15,000 income from sources without the United States which is not effectively connected with the conduct of a trade or business in the United States. During the period of residence from June 1, 1971, to December 31, 1971, A receives wages of $10,000, dividends of $200 from a foreign corporation, and dividends of $75 from a domestic corporation qualifying under section 116(a). Of the amount of wages so received, $2,000 is for services performed by A outside the United States during the period of nonresidence. Total allowable deductions (other than for personal exemptions) amount to $700, none of which are deductible under section 62 in computing adjusted gross income. For 1971 A's spouse has no gross income and is not the dependent of another taxpayer. For 1971, A's taxable income is $8,200, all of which is subject to tax under section 1, as follows:

Wages		$10,000
Dividends from foreign corporation		200
Dividends from domestic corporation ($75 less $75 exclusion)		0
Adjusted gross income		10,200
Less deductions:		
Personal exemptions (2×$650)	$1,300	
Other allowable deductions	700	2,000
Taxable income		8,200

Example (2). The facts are the same as in example (1) except that during the period of nonresidence from January 1, 1971, to May 31, 1971, A receives from sources within the United States income of $1,850 which is effectively connected with the conduct by A of a business in the United States and $350 in dividends from domestic corporations qualifying under section 116(a). Only $50 of these dividends are effectively connected with the conduct by A of a business in the United States. The assumption is made that there are no allowable deductions connected with such effectively connected income. For 1971, A has taxable income of $10,075 subject to tax under section 1 and $300 income subject to tax under section 871(a)(1)(A), as follows:

Wages		$10,000
Business income		1,850
Dividends from foreign corporation		200
Dividends from domestic corporation ($125 less $100 exclusion)		25
Adjusted gross income		12,075
Less deductions:		
Personal exemptions (2×$650)	$1,300	
Other allowable deductions	700	2,000
Taxable income subject to tax under section 1		10,075
Income subject to tax under section 871(a)(1)(A)		300

Example (3). A, a married alien individual with three children, uses the calendar year as the taxable year and the cash receipts and disbursements method of accounting. On October 1, 1971, A and his family become residents of the United States. During the period of nonresidence from January 1, 1971, to September 30, 1971, A receives income of $18,000 from sources without the United States which is not effectively connected with the conduct of a trade or business in the United States and of $2,500 from sources within the United States which is effectively connected with the conduct of a business in the United States. It is assumed there are no allowable deductions connected with such effectively connected income. During the period of residence from October 1, 1971, to December 31, 1971, A receives wages of $2,000, of which $400 is for services performed outside the United States during the period of nonresidence. Total allowable deductions (other than for personal exemptions) amount to $250, none of which are deductible under section 62 in computing adjusted gross income. Neither the spouse nor any of the children has any gross income for 1971, and the spouse is not the dependent of another taxpayer for such year. For 1971, A's taxable income is $1,850, all of which is subject to tax under section 1, as follows:

Wages (residence period)	$2,000	
Less: Allowable deductions	250	
Taxable income (without deduction for personal exemptions) (residence period)		$1,750
Business income (nonresidence period)		2,500
Total taxable income (without deduction for personal exemptions)		4,250
Less deduction for personal exemptions:		
Taxpayer	650	
Wife and 3 children (4×$650, but not to exceed $1,750)	1,750	
		2,400
Taxable income		1,850

(f) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. There are no corresponding rules in this part for taxable years beginning before January 1, 1967.

§ 1.871–8 [Deleted]

PAR. 13. Section 1.871–8 is deleted.

PAR. 14 Section 1.872 is amended by revising sections 872 (a) and (b)(3)(B), by adding a new paragraph (4) at the end of section 872(b), and by revising the historical note. These amended and added provisions read as follows:

§ 1.872 **Statutory provisions; gross income.**

SEC. 872. *Gross income*—(a) *General rule.* In the case of a nonresident alien individual, gross income includes only—

(1) Gross income which is derived from sources within the United States and which is not effectively connected with the conduct of a trade or business within the United States, and

(2) Gross income which is effectively connected with the conduct of a trade or business within the United States.

(b) *Exclusions.* * * *

(3) *Compensation of participants in certain exchange or training programs.* * * *

(B) An office or place of business maintain in a foreign country or in a possession of the United States by a domestic corporation, a domestic partnership, or an individual who is a citizen or resident of the United States.

(4) *Certain bond income of residents of the Ryukyu Islands or the Trust Territory of the Pacific Islands.* Income derived by a nonresident alien individual from a series E or series H U.S. savings bond, if such individual acquired such bond while a resident of the Ryukyu Island or the Trust Territory of the Pacific Islands.

[Sec. 872 as amended by sec. 110(c), Mutual Educational and Cultural Exchange Act 1961 (75 Stat. 536); sec. 103(b), Foreign Investors Tax Act 1966 (80 Stat. 1550)]

PAR. 15. Section 1.872-1 is amended to read as follows:

§ 1.872-1 Gross income of nonresident alien individuals.

(a) *In general*—(1) *Inclusions.* The gross income of a nonresident alien individual for any taxable year includes only (i) the gross income which is derived from sources within the United States and which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual and (ii) the gross income, irrespective of whether such income is derived from sources within or without the United States, which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. For the determination of the sources of income, see sections 861 through 863 and the regulations thereunder. For the determination of whether income from sources within or without the United States is effectively connected for the taxable year with the conduct of a trade or business in the United States, see sections 864(c) and 871 (c) and (d), §§ 1.864-3 through 1.864-7, and §§ 1.871-9 and 1.871-10. For special rules for determining the income of an alien individual who changes his residence during the taxable year, see § 1.871-13.

(2) *Exchange transactions.* Even though a nonresident alien individual who effects certain transactions in the United States in stocks, securities, or commodities during the taxable year may not, by reason of section 864(b)(2) and paragraph (c) or (d) of § 1.864-2, be engaged in trade or business in the United States during the taxable year through the effecting of such transactions, nevertheless he shall be required to include in gross income for the taxable year the gains and profits from those transactions to the extent required by § 1.871-7 or § 1.871-8.

(3) *Exclusions.* For exclusions from gross income, see § 1.872-2.

(b) *Individuals not engaged in U.S. business.* In the case of a nonresident alien individual who at no time during the taxable year is engaged in trade or business in the United States, the gross income shall include only (1) the gross income from sources within the United States which is described in section 871 (a) and paragraphs (b), (c), and (d) of § 1.871-7, and (2) the gross income from sources within the United States which, by reason of section 871 (c) or (d) and § 1.871-9 or § 1.871-10, is treated as effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual.

(c) *Individuals engaged in U.S. business.* In the case of a nonresident alien individual who is engaged in trade or business in the United States at any time during the taxable year, the gross income shall include (1) the gross income from sources within and without the United States which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, (2) the gross income from sources within the United States which, by reason of the election provided in section 871(d) and § 1.871-10, is treated as effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual, and (3) the gross income from sources within the United States which is described in section 871(a) and paragraphs (b), (c), and (d) of § 1.871-7 and is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual.

(d) *Special rules applicable to certain expatriates.* For special rules for determining the gross income of a nonresident alien individual who has lost U.S. citizenship with a principal purpose of avoiding certain taxes, see section 877 (b)(1).

(e) *Alien resident of Puerto Rico.* This section shall not apply in the case of a nonresident alien individual who is a bona fide resident of Puerto Rico during the entire taxable year. See section 876 and § 1.876-1.

(f) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.872-1 (Rev. as of Jan. 1, 1971).

PAR. 16. Section 1.872-2 is amended to read as follows:

§ 1.872-2 Exclusions from gross income of nonresident alien individuals.

(a) *Earnings of foreign ships or aircraft*—(1) *Basic rule.* So much of the income from sources within the United States of a nonresident alien individual as consists of earnings derived from the operation of a ship or ships documented, or of aircraft registered, under the laws of a foreign country which grants an equivalent exemption to citizens of the United States nonresident in that foreign country and to corporations organized in the United States shall not be included in gross income.

(2) *Equivalent exemption*—(i) *Ships.* A foreign country which either imposes no income tax, or, in imposing an income tax, exempts from taxation so much of the income of a citizen of the U.S. nonresident in that foreign country and of a corporation organized in the United States as consists of earnings derived from the operation of a ship or ships documented under the laws of the United States is considered as granting an equivalent exemption for purposes of the exclusion from gross income of the earnings of a foreign ship or ships.

(ii) *Aircraft.* A foreign country which either imposes no income tax, or, in imposing an income tax, exempts from taxation so much of the income of a citizen of the U.S. nonresident in that foreign country and of a corporation organized in the United States as consists of earnings derived from the operation of aircraft registered under the laws of the United States is considered as granting an equivalent exemption for purposes of the exclusion from gross income of the earnings of foreign aircraft.

(3) *Definition of earnings.* For purposes of subparagraphs (1) and (2) of this paragraph, compensation for personal services performed by an individual aboard a ship or aircraft does not constitute earnings derived by such individual from the operation of ships or aircraft.

(b) *Compensation paid by foreign employer to participants in certain exchange or training programs*—(1) *Exclusion from income.* Compensation paid to a nonresident alien individual for the period that the nonresident alien individual is temporarily present in the United States as a nonimmigrant under subparagraph (F) (relating to the admission of students into the United States) or subparagraph (J) (relating to the admission of teachers, trainees, specialists, etc., into the United States) of section 101(a)(15) of the Immigration and Nationality Act (8 U.S.C. 1101(a)(15) (F) or (J)) shall be excluded from gross income if the compensation is paid to such alien by his foreign employer. Compensation paid to a nonresident alien individual by the U.S. office of a domestic bank which is acting as paymaster on behalf of a foreign employer constitutes compensation paid by a foreign employer for purposes of this paragraph if the domestic bank is reimbursed by the foreign employer for such payment. A nonresident alien individual who is temporarily present in the United States as a nonimmigrant under such subparagraph (J) includes a nonresident alien individual admitted to the United States as an "exchange visitor" under section 201 of the U.S. Information and Educational Exchange Act of 1948 (22 U.S.C. 1446), which section was repealed by section 111 of the Mutual Education and Cultural Exchange Act of 1961 (75 Stat. 538).

(2) *Definition of foreign employer.* For purposes of this paragraph, the term "foreign employer" means a nonresident alien individual, a foreign partnership, a foreign corporation, or an office or place of business maintained in a foreign country or in a possession of the United States by a domestic corporation, a

domestic partnership, or an individual who is a citizen or resident of the United States. The term does not include a foreign government. However, see section 893 and § 1.893-1. Thus, if a French citizen employed in the Paris branch of a banking company incorporated in the State of New York were admitted to the United States under section 101(a)(15)(J) of the Immigration and Nationality Act to study monetary theory and continued to receive a salary from such foreign branch while studying in the United States, such salary would not be includable in his gross income.

(c) *Tax convention*. Income of any kind which is exempt from tax under the provisions of a tax convention or treaty to which the United States is a party shall not be included in the gross income of a nonresident alien individual. Income on which the tax is limited by tax convention shall be included in the gross income of a nonresident alien individual if it is not otherwise excluded from gross income. See §§ 1.871-12 and 1.894-1.

(d) *Certain bond income of residents of the Ryukyu Islands or the Trust Territory of the Pacific Islands*. Income derived by a nonresident alien individual from a series E or series H U.S. savings bond shall not be included in gross income if such individual acquired the bond while he was a resident of the Ryukyu Islands or the Trust Territory of the Pacific Islands. It is not necessary that the individual continue to be a resident of such Islands or Trust Territory for the period when, without regard to section 872(b)(4) and this paragraph, the income from the bond would otherwise be includible in his gross income under the provisions of section 446 or 454.

(e) *Certain annuities received under qualified plans*. Pursuant to section 871(f), income received by a nonresident alien individual as an annuity under a qualified annuity plan described in section 403(a)(1) (relating to taxation of employee annuities), or from a qualified trust described in section 401(a) (relating to qualified pension, profit-sharing, and stock bonus plans) which is exempt from tax under section 501(a) (relating to exemption from tax on corporations, certain trusts, etc.), shall not be included in gross income, and shall be exempt from tax, for purposes of section 871 and §§ 1.871-7 and 1.871-8, if—

(1) All of the personal services by reason of which the annuity is payable were either—

(i) Personal services performed outside the United States by an individual (whether or not the annuitant) who, at the time of performance of the services, was a nonresident alien individual, or

(ii) Personal services performed in the United States by a nonresident alien individual (whether or not the annuitant) which, by reason of section 864(b)(1) (or corresponding provision of any prior law), were not personal services causing such individual to be engaged in trade or business in the United States during the taxable year, and

(2) At the time the first amount is paid (even though paid in a taxable year beginning before January 1, 1967) as such annuity under such annuity plan, or by such trust, to (i) the individual described in subparagraph (1) of this paragraph, or (ii) his nonresident alien beneficiary if such beneficiary is entitled to receive such first amount, 90 percent or more of the employees or annuitants for whom contributions or benefits are provided under the annuity plan, or under the plan or plans of which the trust is a part, are citizens or residents of the United States.

This paragraph shall apply whether or not the taxpayer is engaged in trade or business in the United States at any time during the taxable year in which the annuity is received. This paragraph shall not apply to distributions by an employees' trust or from an annuity plan which give rise to gains described in section 402(a)(2) or 403(a)(2), whichever applies. See section 871(a)(1)(B) and paragraph (c)(1)(i) of § 1.871-7. For exemption from withholding of tax at source on an annuity which is exempt from tax under section 871(f) and this paragraph, see paragraph (g) of § 1.1441-4.

(f) *Other exclusions*. Income which is from sources without the United States, as determined under the provisions of sections 861 through 863, and the regulations thereunder, is not included in the gross income of a nonresident alien individual unless such income is effectively connected for the taxable year with the conduct of a trade or business in the United States by that individual. To determine specific exclusions in the case of other items which are from sources within the United States, see the applicable sections of the Code. For special rules under a tax convention for determining the sources of income and for excluding, from gross income, income from sources without the United States which is effectively connected with the conduct of a trade or business in the United States, see the applicable tax convention. For determining which income from sources without the United States is effectively connected with the conduct of a trade or business in the United States, see section 864(c)(4) and § 1.864-5.

(g) *Effective date*. This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 4, 1967 see 26 CFR 1.872-2 (Rev. as of Jan. 1, 1971).

PAR. 17. Section 1.876-1 is amended by revising paragraphs (b) and (c) and by adding a new paragraph (d). These amended and added provisions read as follows:

§ 1.876-1 Alien residents of Puerto Rico.

* * * * *

(b) *Exceptions*. Though subject to the tax imposed by section 1, a nonresident alien individual who is a bona fide resident of Puerto Rico during his entire taxable year shall nevertheless be treated as a nonresident alien individual for the purpose of many provisions of the Code relating to nonresident alien individuals. Thus, for example, such a resident of Puerto Rico is not allowed to determine his tax in accordance with the optional tax table (section 4(d)(1)); is not allowed the standard deduction (section 142(b)(1); is not allowed a deduction for a "dependent" who is a resident of Puerto Rico unless the dependent is a citizen of the United States (section 152(b)(3)); is subject to withholding of tax at source under chapter 3 of the Code (sections 1441(e) and 1451(e)); is generally excepted from the collection of income tax at source on wages (paragraph (d)(1) of § 31.3401(a)(6)-1 of this chapter (Employment Tax Regulations)); is not allowed to make a joint return or a joint declaration of estimated tax (sections 6013(a)(1) and 6015(b)); must pay his estimated income tax on or before the 15th day of the 4th month of the taxable year (sections 6015(i)(3), 6073(a), and 6153(a)(1)); and generally must pay his income tax on or before the 15th day of the 6th month following the close of the taxable year (sections 6072(c) and 6151(a)).

(c) *Credits against tax*. The credits allowed by section 31 (relating to tax withheld on wages), section 32 (relating to tax withheld at source on nonresident alients), section 33 (relating to taxes of foreign countries), section 35 (relating to partially tax-exempt interest), section 38 (relating to investment in certain depreciable property), section 39 (relating to certain uses of gasoline and lubricating oil), and section 40 (relating to expenses of work incentive programs) shall be allowed against the tax determined in accordance with this section. No credit shall be allowed under section 37 in respect of retirement income.

(d) *Effective date*. This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.876-1 (Rev. as of Jan. 1, 1971).

PAR. 18. Section 1.877 is redesignated as § 1.878 and revised to read as follows:

§ 1.878 Statutory provisions; certain foreign exempt organizations.

SEC. 878. *Foreign educational, charitable, and certain other exempt organizations*. For special provisions relating to foreign educational, charitable, and other exempt organizations, see sections 512(a) and 4948.

[Sec. 878 as redesignated by sec. 103(f)(1), Foreign Investors Tax Act 1966 (80 Stat. 1551); as amended by sec. 101(j)(20), Tax Reform Act 1969 (83 Stat. 528)]

PAR. 19. The following new section is inserted immediately after § 1.876-1:

§ 1.877 Statutory provisions; expatriation to avoid tax.

SEC. 877. *Expatriation to avoid tax*—(a) *In general*. Every nonresident alien individual who at any time after March 8, 1965, and within the 10-year period immediately preceding the close of the taxable year lost U.S. citizenship, unless such loss did not have for one of its principal purposes the avoidance of taxes under this subtitle or subtitle B, shall be taxable for such taxable year in the manner provided in subsection (b) if the tax imposed pursuant to such subsection exceeds the tax which, without regard to this section, is imposed pursuant to section 871.

(b) *Alternative tax.* A nonresident alien individual described in subsection (a) shall be taxable for the taxable year as provided in section 1 or section 1201(b), except that—

(1) The gross income shall include only the gross income described in section 872(a) (as modified by subsection (c) of this section), and

(2) The deductions shall be allowed if and to the extent that they are connected with the gross income included under this section except that the capital loss carryover provided by section 1212(b) shall not be allowed; and the proper allocation and apportionment of the deductions for this purpose shall be determined as provided under regulations prescribed by the Secretary or his delegate.

For purposes of paragraph (2), the deductions allowed by section 873(b) shall be allowed; and the deduction (for losses not connected with the trade or business if incurred in transactions entered into for profit) allowed by section 165(c)(2) shall be allowed, but only if the profit, if such transaction had resulted in a profit, would be included in gross income under this section.

(c) *Special rules of source.* For purposes of subsection (b), the following items of gross income shall be treated as income from sources within the United States:

(1) *Sale of property.* Gains on the sale or exchange of property (other than stock or debt obligations) located in the United States.

(2) *Stock or debt obligations.* Gains on the sale or exchange of stock issued by a domestic corporation or debt obligations of U.S. persons or of the United States, a State or political subdivision thereof, or the District of Columbia.

(d) *Exception for loss of citizenship for certain causes.* Subsection (a) shall not apply to a nonresident alien individual whose loss of U.S. citizenship resulted from the application of section 301(b), 350, or 355 of the Immigration and Nationality Act, as amended (8 U.S.C. 1401(b), 1482, or 1487).

(e) *Burden of proof.* If the Secretary or his delegate establishes that it is reasonable to believe that an individual's loss of U.S. citizenship would, but for this section, result in a substantial reduction for the taxable year in the taxes on his probable income for such year, the burden of proving for such taxable year that such loss of citizenship did not have for one of its principal purposes the avoidance of taxes under this subtitle or subtitle B shall be on such individual.

[Sec. 877 as added by sec. 103(f)(1), Foreign Investors Tax Act 1966 (80 Stat. 1551)]

PAR. 20. Section 1.932 is amended by revising section 932(a) and by adding a historical note as follows:

§ 1.932 Statutory provisions; taxation of citizens of possessions of the United States.

SEC. 932. *Citizens of possessions of the United States*—(a) *General rule.* Any individual who is a citizen of any possession of the United States (but not otherwise a citizen of the United States) and who is not a resident of the United States shall be subject to taxation under this subtitle in the same manner and subject to the same conditions as in the case of a nonresident alien individual. This section shall have no application in the case of a citizen of Puerto Rico.

* * * * *

[Sec. 932 as amended by sec. 103(m), Foreign Investors Tax Act 1966 (80 Stat. 1554)]

PAR. 21. Section 1.932–1 is amended by revising paragraph (a)(1) to read as follows:

§ 1.932–1 Status of citizens of U.S. possessions.

(a) *General rule*—(1) *Definition and treatment.* A citizen of a possession of the United States (except Puerto Rico), who is not otherwise a citizen or resident of the United States, including only the States and the District of Columbia, is treated for the purpose of the taxes imposed by Subtitle A of the Code (relating to income taxes) as if he were a nonresident alien individual. However, for purposes of the tax imposed on self-employment income by chapter 2 of the Code, the term "possession of the United States" as used in section 932 and the preceding sentence does not include American Samoa, Guam, or the Virgin Islands. See section 1402(a)(9). See subpart A (section 871 and following), part II, subchapter N, chapter 1 of the Code, and the regulations thereunder, for rules relating to imposition of tax on nonresident alien individuals. For Federal income tax purposes, a citizen of a possession of the United States who is not otherwise a citizen of the United States is a citizen of a possession of the United States who has not become a citizen of the United States by naturalization in a State, Territory, or the District of Columbia. The fixed or determinable annual or periodical income from sources within the United States of a citizen of a possession of the United States who is treated as if he was a nonresident alien individual is subject to withholding. See section 1441.

* * * * *

PAR. 22. Section 1.1493 is amended by adding a historical note to read as follows:

§ 1.1493 Statutory provisions; definition of foreign trust.

* * * * *

[Sec. 1493 as in effect before its repeal by sec. 103(l)(2), Foreign Investors Tax Act 1966 (80 Stat. 1544)]

PAR. 23. Section 1.1493–1 is revised to read as follows:

§ 1.1493–1 Definition of foreign trust.

For taxable years beginning before January 1, 1967, a trust is to be considered a "foreign trust" within the meaning of chapter 5 of the Code, if, assuming a subsequent sale by the trustee, outside the United States and for cash, of the property transferred to the trust, the profit, if any, from such sale (being income from sources without the United States under the provisions of part I (section 861 and following), subchapter N, chapter 1 of the Code), would not be included in the gross income of the trust under subtitle A of the Code. For taxable years beginning after December 31, 1966, the term "foreign trust," as used in chapter 5 of the Code, shall have the meaning prescribed by section 7701(a)(31).

PAR. 24. Section 1.6012–1 is amended by revising paragraph (b) to read as follows:

§ 1.6012–1 Individuals required to make returns of income.

* * * * *

(b) *Return of nonresident alien individual*—(1) *Requirement of return*—(i) *In general.* Except as otherwise provided in subparagraph (2) of this paragraph, every nonresident alien individual who is engaged in trade or business in the United States at any time during the taxable year or who has income which is subject to taxation under subtitle A of the Code shall make a return on Form 1040NR. For this purpose it is immaterial that the gross income for the taxable year is less than the minimum amount specified in section 6012(a) for making a return. Thus, a nonresident alien individual who is engaged in a trade or business in the United States at any time during the taxable year is required to file a return on Form 1040NR even though (*a*) he has no income which is effectively connected with the conduct of a trade or business in the United States, (*b*) he has no income from sources within the United States, or (*c*) his income is exempt from income tax by reason of an income tax convention or any section of the Code. However, if the nonresident alien individual has no gross income for the taxable year, he is not required to complete the return schedules but must attach a statement to the return indicating the nature of any exclusions claimed and the amount of such exclusions to the extent such amounts are readily determinable.

(ii) *Treaty income.* If the gross income of a nonresident alien individual includes treaty income, as defined in paragraph (b)(1) of § 1.871–12, a statement shall be attached to the return on Form 1040NR showing with respect to that income—

(*a*) The amounts of tax withheld,

(*b*) The names and post office addresses of withholding agents, and

(*c*) Such other information as may be required by the return form, or by the instructions issued with respect to the form, to show the taxpayer's entitlement to the reduced rate of tax under the tax convention.

(2) *Exceptions*—(i) *Return not required when tax is fully paid at source.* A nonresident alien individual who at no time during the taxable year is engaged in a trade or business in the United States is not required to make a return for the taxable year if his tax liability for the taxable year is fully satisfied by the withholding of tax at source under chapter 3 of the Code. This subdivision does not apply to a nonresident alien individual who has income for the taxable year which is treated under section 871 (c) or (d) and § 1.871–9 (relating to students or trainees) or § 1.871–10 (relating to real property income) as income which is effectively connected for the taxable year with the conduct of a trade or business in the

United States by that individual, or to a nonresident alien individual making a claim under § 301.6402-3 of this chapter (Procedure and Administration Regulations) for the refund of an overpayment of tax for the taxable year. For purposes of this subdivision, some of the items of income from sources within the United States upon which the tax liability will not have been fully satisfied by the withholding of tax at source under chapter 3 of the Code are:

(*a*) Interest upon so-called tax-free covenant bonds upon which, in accordance with section 1451 and § 1.1451-1, a tax of only 2 percent is required to be withheld at the source.

(*b*) In the case of bonds or other evidences of indebtedness issued after September 28, 1965, amounts described in section 871(a)(1)(C),

(*c*) Capital gains described in section 871(a)(2) and paragraph (d) of § 1.871-7, and

(*d*) Accrued interest received in connection with the sale of bonds between interest dates, which, in accordance with paragraph (h) of § 1.1441-4, is not subject to withholding of tax at the source.

(ii) *Return of individual for taxable year of change of U.S. citizenship or residence.* (*a*) If an alien individual becomes a citizen or resident of the United States during the taxable year and is a citizen or resident of the United States on the last day of such year, he must make a return on Form 1040 for the taxable year. However, a separate schedule is required to be attached to this return to show the income tax computation for the part of the taxable year during which the alien was neither a citizen nor resident of the United States. A Form 1040NR, clearly marked "Statement" across the top, may be used as such a separate schedule.

(*b*) If an individual abandons his U.S. citizenship or residence during the taxable year and is not a citizen or resident of the United States on the last day of such year, he must make a return on Form 1040NR for the taxable year. However, a separate schedule is required to be attached to this return to show the income tax computation for the part of the taxable year during which the individual was a citizen or resident of the United States. A Form 1040, clearly marked "Statement" across the top, may be used as such a separate schedule.

(*c*) A return is required under this subdivision (ii) only if the individual is otherwise required to make a return for the taxable year.

(iii) *Beneficiaries of estates or trusts.* A nonresident alien individual who is a beneficiary of an estate or trust which is engaged in trade or business in the United States is not required to make a return for the taxable year merely because he is deemed to be engaged in trade or business within the United States under section 875(2). However, such nonresident alien beneficiary will be required to make a return if he otherwise satisfies the conditions of subparagraph (1)(i) of this paragraph for making a return.

(iv) *Certain alien residents of Puerto Rico.* This paragraph does not apply to a nonresident alien individual who is a bona fide resident of Puerto Rico during the taxable year. See section 876 and paragraph (a)(1)(iii) of this section.

(3) *Representative or agent for nonresident alien individual*—(i) *Cases where power of attorney is not required.* The responsible representative or agent within the United States of a nonresident alien individual shall make on behalf of his nonresident alien principal a return of, and shall pay the tax on, all income coming within his control as representative or agent which is subject to the income tax under subtitle A of the Code. The agency appointment will determine how completely the agent is substituted for the principal for tax purposes. Any person who collects interest or dividends on deposited securities of a nonresident alien individual, executes ownership certificates in connection therewith, or sells such securities under special instructions shall not be deemed merely by reason of such acts to be the responsible representative or agent of the nonresident alien individual. If the responsible representative or agent does not have a specific power of attorney from the nonresident alien individual to file a return in his behalf, the return shall be accompanied by a statement to the effect that the representative or agent does not possess specific power of attorney to file a return for such individual but that the return is being filed in accordance with the provisions of this subdivision.

(ii) *Cases where power of attorney is required.* Whenever a return of income of a nonresident alien individual is made by an agent acting under a duly authorized power of attorney for that purpose, the return shall be accompanied by the power of attorney in proper form, or a copy thereof, specifically authorizing him to represent his principal in making, executing, and filing the income tax return. Form 2848 may be used for this purpose. The agent, as well as the taxpayer, may incur liability for the penalties provided for erroneous, false, or fraudulent returns. For the requirements regarding signing of returns, see § 1.6061-1. The rules of paragraph (e) of § 601.504 of this chapter (Statement of Procedural Rules) shall apply under this subparagraph in determining whether a copy of a power of attorney must be certified.

(iii) *Limitation.* A return of income shall be required under this subparagraph only if the nonresident alien individual is otherwise required to make a return in accordance with this paragraph.

(4) *Disallowance of deductions and credits.* For provisions disallowing deductions and credits when a return of income has not been filed by or on behalf of a nonresident alien individual, see section 874(a) and the regulations thereunder.

(5) *Effective date.* This paragraph shall apply for taxable years beginning after December 31, 1966, except that it shall not be applied to require (i) the filing of a return for any taxable year ending before January 1, 1974, which, pursuant to instructions applicable to the return, is not required to be filed or (ii) the amendment of a return for such a taxable year which, pursuant to such instructions, is required to be filed. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.6012-1(b) (Rev. as of Jan. 1, 1967).

* * * * *

PAR. 25. Section 1.6012-3 is amended by revising subparagraph (2) (i), (iii), and (v) of paragraph (b) to read as follows:

§ 1.6012-3 Returns by fiduciaries.

* * * * *

(b) *For other persons.* * * *

(2) *Nonresident alien individuals*—(i) *In general.* A resident or domestic fiduciary or other person charged with the care of the person or property of a nonresident alien individual shall make a return for that individual and pay the tax unless—

(*a*) The nonresident alien individual makes a return of, and pays the tax on, his income for the taxable year,

(*b*) A responsible representative or agent in the United States of the nonresident alien individual makes a return of, and pays the tax on, the income of such alien individual for the taxable year, or

(*c*) The nonresident alien individual has appointed a person in the United States to act as his agent for the purpose of making a return of income and, if such fiduciary is required to file a Form 1041 for an estate or trust of which such alien individual is a beneficiary, such fiduciary attaches a copy of the agency appointment to his return on Form 1041.

* * * * *

(iii) *Disallowance of deductions and credits.* For provisions disallowing deductions and credits when a return of income has not been filed by or on behalf of a nonresident alien individual, see section 874 and the regulations thereunder.

* * * * *

(v) *Cross reference.* For requirements of withholding tax at source on nonresident alien individuals and of returns with respect to such withheld taxes, see §§ 1.1441-1 to 1.1465-1, inclusive.

* * * * *

PAR. 26. Section 1.601a-4 is revised to read as follows:

§ 1.6012-4 Miscellaneous returns.

For returns by regulated investment companies of tax on undistributed capital gain designated for special treatment under section 852(b)(3)(D), see § 1.852-9. For returns with respect to tax withheld on nonresident aliens and foreign corporations and on tax-free convenant bonds, see §§ 1.1461-1 to 1.1465-1, inclusive. For returns of tax on transfers to avoid income tax, see § 1.1494-1. For the requirement of an annual report by persons completing a Government contract, see 26 CFR (1939) 17.16 (Treasury Decision 4906, approved June 23, 1939), and 26 CFR (1939) 16.15 (Treasury Decision 4909, approved June 28, 1939), as made applicable to section 1471 of the 1954 Code by Treasury Decision 6091, approved August 16, 1954 (19 F.R. 5167, C.B. 1954-2, 47). See also § 1.1471-1.

* * * * *

PAR. 28. Section 1.6015(a)-1 is amended by revising paragraph (d), as follows:

§ 1.6015(a)-1 Declaration of estimated income tax by individuals.

* * * * *

(d) *Nonresident alien individuals.* For the rules exempting certain nonresident alien individuals from the requirement of making a declaration of estimated income tax, see § 1.6015(i)-1.

* * * * *

PAR. 29. Section 1.6015(i) is redesignated as § 1.6015(j) and revised to read as follows:

§ 1.6015(j) Statutory provisions; declaration of estimated income tax by individuals; applicability.

SEC. 6015. *Declaration of estimated income tax by individuals.* * * *

(j) *Applicability.* This section shall be applicable only with respect to taxable years beginning after December 31, 1954; and sections 58, 59, and 60 of the Internal Revenue Code of 1939 shall continue in force with respect to taxable years beginning before January 1, 1955.

[Sec. 6015(j) as redesignated by sec. 103(j) (2) Foreign Investors Tax Act (80 Stat. 1554)]

[(b) *Declarations of estimated tax.* In the case of a taxable year beginning before [December 30, 1969], if any taxpayer is required to make a declaration or amended declaration of estimated tax, or to pay any amount or additional amount of estimated tax, by reason of the amendments made by [the Tax Reform Act of 1969], such amount or additional amount shall be paid ratably on or before each of the remaining installment dates for the taxable year beginning with the first installment date on or after [January 29, 1970]. With respect to any declaration or payment of estimated tax before such first installment date, sections 6015 [and] 6654 * * * of the Internal Revenue Code of 1954 shall be applied without regard to the amendments made by [the Tax Reform Act of 1969]. For purposes of this subsection, the term "installment date" means any date on which, under section 6153 * * * of such Code * * *, an installment payment of estimated tax is required to be made by the taxpayer. (Sec. 946(b), Tax Reform Act 1969 (83 Stat. 729))]

§ 1.6015(j)-1 [Redesignated]

PAR. 30. Section 1.6015(i)-1 is redesignated as § 1.6015(j)-1.

PAR. 31. The following new sections are inserted immediately after § 1.6015 (h)-1:

§ 1.6015(i) Statutory provisions; declaration of estimated income tax by individuals; nonresident alien individuals.

(i) *Nonresident alien individuals.* No declaration shall be required to be made under this section by a nonresident alien individual unless—

(1) Withholding under chapter 24 is made applicable to the wages, as defined in section 3401(a), of such individual,

(2) Such individual has income (other than compensation for personal services subject to deduction and withholding under section 1441) which is effectively connected with the conduct of a trade or business within the United States, or

(3) Such individual is a resident of Puerto Rico during the entire taxable year.

[Sec. 6015(i) as added by sec. 103(j)(3), Foreign Investors Tax Act 1966 (80 Stat. 1554)]

§ 1.6015(i)-1 Nonresident alien individuals.

(a) *Exception from requirement of making a declaration.* No declaration of estimated income tax is required to be made under section 6015(a) and § 1.6015(a)-1 by a nonresident alien individual unless—

(1) Such individual has wages, as defined in section 3401(a), and the regulations thereunder, upon which tax is required to be withheld under section 3402,

(2) Such individual has income (other than compensation for personal services upon which tax is required to be withheld at source under section 1441) which is effectively connected for the taxable year with the conduct of a trade or business in the United States by such individual, or

(3) Such individual has been, or expects to be, a resident of Puerto Rico during the entire taxable year.

(b) *Rules applicable to nonresident alien individuals required to make a declaration*—(1) *Tests to be applied.* A nonresident alien individual who is not excepted by paragraph (a) of this section from the requirement of making a declaration of income tax is required to file a declaration if his gross income meets the requirements of section 6015(a) and § 1.6015(a)-1. In making the determination under section 6015 (a)(1) as to whether the amount of the gross income of a nonresident alien individual is such as to require making a declaration of estimated income tax, only the tests relating to a single individual (other than a head of household) or to a married individual not entitled to file a joint declaration with his spouse shall apply, since a nonresident alien individual may not make a joint declaration by reason of section 6015(b) and is not a head of household. Only in a rare case would a nonresident alien individual be a surviving spouse.

(2) *Determination of gross income.* To determine the gross income of a nonresident alien individual who is not, or does not expect to be, a resident of Puerto Rico during the entire taxable year, see section 872 and §§ 1.872-1 and 1.872-2. To determine the gross income of a nonresident alien individual who is, or expects to be, a resident of Puerto Rico during the entire taxable year, see section 876 and § 1.876-1. For purposes of applying paragraph (a)(2) of this section, income which is effectively connected for the taxable year with the conduct of a trade or business in the United States includes all income which is treated under section 871 (c) or (d) and § 1.871-9 (relating to students and trainees) or § 1.871-10 (relating to real property income) as income which is effectively connected for such year with the conduct of a trade or business in the United States.

(c) *Effective date.* This section shall apply for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.6015(a)-1(d) (Rev. as of Jan. 1, 1971).

PAR. 32. Section 1.6061-1 is amended to read as follows:

§ 1.6061-1 Signing of returns and other documents by individuals.

(a) *Requirement.* Each individual (including a fiduciary) shall sign the income tax return required to be made by him, except that the return may be signed for the taxpayer by an agent who is duly authorized in accordance with paragraph (a)(5) or (b) of § 1.6012-1 to make such return. Other returns, statements, or documents required under the provisions of subtitle A or F of the Code or of the regulations thereunder to be made by any person with respect to any tax imposed by subtitle A of the Code shall be signed in accordance with any regulations contained in this chapter, or any instructions, issued with respect to such returns, statements, or other documents.

(b) *Cross references.* For provisions relating to the signing of returns, statements, or other documents required to be made by corporations and partnerships with respect to any tax imposed by subtitle A of the Code, see §§ 1.6062-1 and 1.6063-1, respectively. For provisions relating to the making of returns by agents, see paragraphs (a)(5) and (b) of § 1.6012-1; and to the making of returns for minors and persons under a disability, see paragraph (a)(4) of § 1.6012-1 and paragraph (b) of § 1.6012-3.

Par. 18. Section 1.703-1 is amended by adding at the end of paragraph (b)(2) the following new subdivision:

§ 1.703-1 Partnership computations.

* * * * *

(b) *Elections of the partnership.* * * *

(2) *Exceptions.* * * *

(iii) Each partner who is a nonresident alien individual or a foreign corporation shall add his distributive share of income derived by the partnership from real property located in the United States, as described in section 871(d)(1) or 882(d)(1), to any such income derived by him and may elect under § 1.871-10 to treat all such income as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States.

Par. 19. Section 1.864-4 is amended by revising paragraph (c) (3) (i) to read as follows:

§ 1.864-4 U.S. source income effectively connected with U.S. business.

* * * * *

(c) *Fixed or determinable income and capital gains.* * * *

(3) *Application of the business-activities test*—(i) *In general*. For purposes of subparagraph (1) of this paragraph, the business-activities test shall ordinarily apply in making a determination with respect to income, gain, or loss which, even though generally of the passive type, arises directly from the active conduct of the taxpayer's trade or business in the United States. The business-activities test is of primary significance, for example, where (*a*) dividends or interest are derived by a dealer in stocks or securities, (*b*) gain or loss is derived from the sale or exchange of capital assets in the active conduct of a trade or business by an investment company, (*c*) royalties are derived in the active conduct of a business consisting of the licensing of patents or similar intangible property, or (*d*) service fees are derived in the active conduct of a servicing business. In applying the business-activities test, activities relating to the management of investment portfolios shall not be treated as activities of the trade or business conducted in the United States unless the maintenance of the investments constitutes the principal activity of that trade or business. See also subparagraph (5) of this paragraph for rules applicable to taxpayers conducting a banking, financing, or similar business in the United States.

* * * * *

PAR. 20. The following new section is added immediately after § 1.875-1:

§ 1.875-2 Beneficiaries of estates or trusts.

(a) [Reserved]

(b) *Exception for certain taxable years*. Notwithstanding paragraph (a) of this section, for any taxable year beginning before January 1, 1975, the grantor of a trust, whether revocable or irrevocable, is not deemed to be engaged in trade or business within the United States merely because the trustee is engaged in trade or business within the United States.

(c) [Reserved]

PAR. 21. Section 1.912 is amended to read as follows:

§ 1.912 Statutory provisions; exemptions for certain allowances.

SEC. 912. *Exemptions for certain allowances*. The following items shall not be included in gross income, and shall be exempt from taxation under this subtitle:

(1) *Foreign areas allowances*. In the case of civilian officers and employees of the Government of the United States, amounts received as allowances or otherwise (but not amounts received as post differentials) under—

(A) Title IX of the Foreign Service Act of 1946, as amended (22 U.S.C., sec. 1131 and following),

(B) Section 4 of the Central Intelligence Agency Act of 1949, as amended (50 U.S.C., sec. 403e),

(C) Title II of the Overseas Differentials and Allowances Act, or

(D) Subsection (e) or (f) of the first section of the Administrative Expenses Act of 1946, as amended, or section 22 of such Act.

(2) *Cost-of-living allowances*. In the case of civilian officers or employees of the Government of the United States stationed outside the continental United States (other than Alaska), amounts (other than amounts received under title II of the Overseas Differentials and Allowances Act) received as cost-of-living allowances in accordance with regulations approved by the President.

(3) *Peace corps allowances*. In the case of an individual who is a volunteer or volunteer leader within the meaning of the Peace Corps Act and members of his family, amounts received as allowances under section 5 or 6 of the Peace Corps Act other than amounts received as—

(A) Termination payments under section 5(c) or section 6(1) of such Act,

(B) Leave allowances,

(C) If such individual is a volunteer leader training in the United States, allowances to members of his family, and

(D) Such portion of living allowances as the President may determine under the Peace Corps Act as constituting basic compensation.

[Sec. 912 as amended by sec. 523(a), Overseas Differentials and Allowances Act (74 Stat. 802); sec. 201(a), Peace Corps Act (75 Stat. 625)]

PAR. 22. Section 1.6012-2 is amended by revising paragraph (g)(5) to read as follows:

§ 1.6012-2 Corporations required to make returns of income.

* * * * *

(g) *Returns by foreign corporations*. * * *

(5) *Effective date*. This paragraph shall apply for taxable years beginning after December 31, 1966, except that it shall not be applied to require (i) the filing of a return for any taxable year ending before January 1, 1974, which, pursuant to instructions applicable to the return, is not required to be filed or (ii) the amendment of a return for such a taxable year which, pursuant to such instructions, is required to be filed. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.6012-2(g) (Rev. as of Jan. 1, 1967).

REGULATIONS ON PROCEDURE AND ADMINISTRATION

PAR. 23. Section 301.6015 is amended by revising subsection (c) of section 6015, by redesignating subsection (i) of section 6015 as subsection (j), by adding a new subsection (i) to section 6015 immediately after subsection (h), and by revising the historical note, as follows:

§ 301.6015 Statutory provisions; declaration of estimated income tax by individuals.

SEC. 6015. *Declaration of estimated income tax by individuals*. * * *

(c) *Estimated tax*. For purposes of this title, in the case of an individual, the term "estimated tax" means—

(1) The amount which the individual estimates as the amount of the income tax imposed by chapter 1 for the taxable year (other than the tax imposed by section 56) plus

(2) The amount which the individual estimates as the amount of the self-employment tax imposed by chapter 2 for the taxable year, minus

(3) The amount which the individual estimates as the sum of any credits against tax provided by part IV of subchapter A of chapter 1.

* * * * *

(i) *Nonresident alien individuals*. No declaration shall be required to be made under this section by a nonresident alien individual unless—

(1) Withholding under chapter 24 is made applicable to the wages, as defined in section 3401(a), of such individual,

(2) Such individual has income (other than compensation for personal services subject to deduction and withholding under section 1441) which is effectively connected with the conduct of a trade or business within the United States, or

(3) Such individual is a resident of Puerto Rico during the entire taxable year.

(j) *Applicability*. This section shall be applicable only with respect to taxable years beginning after December 31, 1954; and sections 58, 59, and 60 of the Internal Revenue Code of 1939 shall continue in force with respect to taxable years beginning before January 1, 1955.

[Sec. 6015 as amended by sec. 74, Technical Amendments Act 1958 (72 Stat. 1660); sec. 5(a), Act of Sept. 14, 1960 (Pub. Law 86-779, 74 Stat. 1000); sec. 1(a)(1), Act of Sept. 25, 1962 (Pub. Law 87-682, 76 Stat. 575); sec. 102(a) Tax Adjustment Act 1966 (80 Stat. 62); sec. 103(j), Foreign Investors Tax Act 1966 (80 Stat. 1554); secs. 301(b)(12), 803(d)(7) and 944, Tax Reform Act 1969 (83 Stat. 586, 684, 729); sec. 209, Rev. Act 1971 (85 Stat. 517)]

[(b) *Declarations of estimated tax*. In the case of a taxable year beginning before [December 30, 1969], if any taxpayer is required to make a declaration or amended declaration of estimated tax, or to pay any amount or additional amount of estimated tax, by reason of the amendments made by [the Tax Reform Act of 1969], such amount or additional amount shall be paid ratably on or before each of the remaining installment dates for the taxable year beginning with the first installment date on or after [January 29, 1970]. With respect to any declaration or payment of estimated tax before such first installment date, sections 6015 [and] 6654 * * * of the Internal Revenue Code of 1954 shall be applied without regard to the amendments made by [the Tax Reform Act of 1969]. For purposes of this subsection, the term "installment date" means any date on which, under section 6153 * * * of such Code * * *, an installment payment of estimated tax is required to be made by the taxpayer. (sec. 946(b), Tax Reform Act 1969 (83 Stat. 729))]

PAR. 24. Section 301.6015-1 is amended to read as follows:

§ 301.6015-1 Declaration of estimated income tax by individuals.

For provisions relating to requirement of declarations of estimated income tax by individuals, see §§ 1.6015(a)-1 to 1.6015(j)-1, inclusive, of this chapter (Income Tax Regulations).

* * * * *

PAR. 33. Section 301.7701 is amended by revising section 7701(a)(20), by adding paragraphs (30), (31), (33), and (34) to section 7701(a), and by revising the historical note. These amended and added provisions read as follows:

§ 301.7701 Statutory provisions; definitions.

Sec. 7701. *Definitions.* (a) When used in this title where not otherwise distinctly expressed or manifest incompatible with the intent thereof—

* * * * *

(20) *Employee.* For the purpose of applying the provisions of section 79 with respect to group-term life insurance purchased for employees, for the purpose of applying the provisions of sections 104, 105, and 106 with respect to accident and health insurance or accident and health plans, for the purpose of applying the provisions of section 101(b) with respect to employees' death benefits, and for the purpose of applying the provisions of subtitle A with respect to contributions to or under a stock bonus, pension, profit-sharing, or annuity plan, and with respect to distributions under such a plan, or by a trust forming part of such a plan, the term "employee" shall include a full-time life insurance salesman who is considered an employee for the purpose of chapter 21, or in the case of services performed before January 1, 1951, who would be considered an employee if his services were performed during 1951.

* * * * *

(30) *U.S. person.* The term "United States person" means—

(A) A citizen or resident of the United States,

(B) A domestic partnership,

(C) A domestic corporation, and

(D) Any estate or trust (other than a foreign estate or foreign trust, within the meaning of section 7701(a)(31)).

(31) *Foreign estate or trust.* The terms "foreign estate" and "foreign trust" mean an estate or trust, as the case may be, the income of which, from sources without the United States which is not effectively connected with the conduct of a trade or business within the United States, is not includible in gross income under subtitle A.

* * * * *

(33) *Regulated public utility.* The term "regulated public utility" means—

(A) A corporation engaged in the furnishing or sale of—

(i) Electric energy, gas, water, or sewerage disposal services, or

(ii) Transportation (not included in subparagraph (C)) on an intrastate, suburban, municipal, or interurban electric railroad, on an intrastate, municipal, or suburban trackless trolley system, or on a municipal or suburban bus system, or

(iii) Transportation (not included in clause (ii)) by motor vehicle—

if the rates for such furnishing or sale, as the case may be, have been established or approved by a State or political subdivision thereof, by an agency or instrumentality of the United States, by a public service or public utility commission or other similar body of the District of Columbia or of any State or political subdivision thereof, or by a foreign country or an agency or instrumentality or political subdivision thereof.

(B) A corporation engaged as a common carrier in the furnishing or sale of transportation of gas by pipeline, if subject to the jurisdiction of the Federal Power Commission.

(C) A corporation engaged as a common carrier (i) in the furnishing or sale of transportation by railroad, if subject to the jurisdiction of the Interstate Commerce Commission, or (ii) in the furnishing or sale of transportation of oil or other petroleum products (including shale oil) by pipeline, if subject to the jurisdiction of the Interstate Commerce Commission or if the rates for such furnishing or sale are subject to the jurisdiction of a public service or public utility commission or other similar body of the District of Columbia or of any State.

(D) A corporation engaged in the furnishing or sale of telephone or telegraph service, if the rates for such furnishing or sale meet the requirements of subparagraph (A).

(E) A corporation engaged in the furnishing or sale of transportation as a common carrier by air, subject to the jurisdiction of the Civil Aeronautics Board.

(F) A corporation engaged in the furnishing or sale of transportation by common carrier by water, subject to the jurisdiction of the Interstate Commerce Commission under part III of the Interstate Commerce Act, or subject to the jurisdiction of the Federal Maritime Board under the Intercoastal Shipping Act of 1933.

(G) A railroad corporation subject to part I of the Interstate Commerce Act, if (i) substantially all of its railroad properties have been leased to another such railroad corporation or corporations by an agreement or agreements entered into before January 1, 1954, (ii) each lease is for a term of more than 20 years, and (iii) at least 80 percent or more of its gross income (computed without regard to dividends and capital gains and losses) for the taxable year is derived from such leases and from sources described in subparagraphs (A) through (F), inclusive. For purposes of the preceding sentence, an agreement for lease of railroad properties entered into before January 1, 1954, shall be considered to be a lease including such term as the total number of years of such agreement may, unless sooner terminated, be renewed or continued under the terms of the agreement, and any such renewal or continuance under such agreement shall be considered part of the lease entered into before January 1, 1954.

(H) A common parent corporation which is a common carrier by railroad subject to part I of the Interstate Commerce Act if at least 80 percent of its gross income (computed without regard to capital gains or losses) is derived directly or indirectly from sources described in subparagraphs (A) through (F), inclusive. For purposes of the preceding sentence, dividends and interest, and income from leases described in subparagraph (G), received from a regulated public utility shall be considered as derived from sources described in subparagraphs (A) through (F), inclusive, if the regulated public utility is a member of an affiliated group (as defined in section 1504) which includes the common parent corporation.

The term "regulated public utility" does not (except as provided in subparagraphs (G) and (H)) include a corporation described in subparagraphs (A) through (F), inclusive, unless 80 percent or more of its gross income (computed without regard to dividends and capital gains and losses) for the taxable year is derived from sources described in subparagraphs (A) through (F), inclusive. If the taxpayer establishes to the satisfaction of the Secretary or his delegate that (i) its revenue from regulated rates described in subparagraph (A) or (D) and its revenue derived from unregulated rates are derived from the operation of a single interconnected and coordinated system or from the operation of more than one such system, and (ii) the unregulated rates have been and are substantially as favorable to users and consumers as are the regulated rates, then such revenue from such unregulated rates shall be considered, for purposes of the preceding sentence, as income derived from sources described in subparagraph (A) or (D).

(34) *Estimated income tax.* The term "estimated income tax" means—

(A) In the case of an individual, the estimated tax as defined in section 6015(c), or

(B) In the case of a corporation, the estimated tax as defined in section 6154(c).

[Sec. 7701 as amended by sec. 22 (g) and (h), Alaska Omnibus Act (73 Stat. 146, 147); sec. 18 (i) and (j), Hawaii Omnibus Act (74 Stat. 416); sec. 103(t), Social Security Amendments 1960 (74 Stat. 941); secs. 6(c) and 7(h), Rev. Act 1962 (76 Stat. 982, 988); sec. 5, Act of Oct. 23, 1962 (Pub. Law 87-870, 76 Stat. 1161); secs. 204(a)(3) and 234 (b) (3), Rev. Act 1964 (78 Stat. 36, 114); sec. 102(b)(5), Tax Adjustment Act 1966 (80 Stat. 64); sec. 103(l)(1), Foreign Investors Tax Act 1966 (80 Stat. 1554); sec. 103 (e) (6), Revenue and Expenditure Control Act 1968 (82 Stat. 264)]

[FR Doc.74-29866 Filed 12-20-74;8:45 am]