

#### 905. Applicable rules

(a) Year in which credit taken. -- The credits provided in this subpart may, at the option of the taxpayer and irrespective of the method of accounting employed in keeping his books, be taken in the year in which the taxes of the foreign country or the possession of the United States accrued, subject, however, to the conditions prescribed in subsection (c). If the taxpayer elects to take such credits in the year in which the taxes of the foreign country or the possession of the United States accrued, the credits for all subsequent years shall be taken on the same basis, and no portion of any such taxes shall be allowed as a deduction in the same or any succeeding year.

(b) Proof of credits. -- The credits provided in this subpart shall be allowed only if the taxpayer establishes to the satisfaction of the Secretary --

(1) the total amount of income derived from sources without the United States, determined as provided in part I,

(2) the amount of income derived from each country, the tax paid or accrued to which is claimed as a credit under this subpart, such amount to be determined under regulations prescribed by the Secretary, and

(3) all other information necessary for the verification and computation of such credits.

(c) Adjustments on payment of accrued taxes. -- If accrued taxes when paid differ from the amounts claimed as credits by the taxpayer, or if any tax paid is refunded in whole or in part, the taxpayer shall notify the Secretary, who shall redetermine the amount of the tax for the year or years affected. The amount of tax due on such redetermination, if any, shall be paid by the taxpayer on notice and demand by the Secretary, or the amount of tax overpaid, if any, shall be credited or refunded to the taxpayer in accordance with subchapter B of chapter 66 (sec. 6511 and following). In the case of such a tax accrued but not paid, the Secretary, as a condition precedent to the allowance of this credit, may require the taxpayer to give a bond, with sureties satisfactory to and to be approved by the Secretary, in such sum as the Secretary may require, conditioned on the payment by the taxpayer of any amount of tax found due on any such redetermination; and the bond herein prescribed shall contain such further conditions as the Secretary may require. In such determination by the Secretary of the amount of tax due from the taxpayer for the year or years affected by a refund, the amount of the taxes refunded for which credit has been allowed under this section shall be reduced by the amount of any tax described in section 901 imposed by the foreign country or possession of the United States with respect to such refund; but not credit under this subpart, and no deduction under section 164 (relating to deduction for taxes) shall be allowed for any taxable year with respect to such tax imposed on the refund. No interest shall be assessed or collected on any amount of tax due on any redetermination by the Secretary, resulting from a refund to the taxpayer, for any period before the receipt of such refund, except to the extent interest was paid by the foreign country or possession of the United States on such refund for such period.

906. Nonresident alien individuals and foreign corporations

(a) Allowance of credit. -- A nonresident alien individual or a foreign corporation engaged in trade or business within the United States during the taxable year shall be allowed a credit under section 901 for the amount of any income, war profits, and excess profits taxes paid or accrued during the taxable year (or deemed, under section 902, paid or accrued during the taxable year) to any foreign country or possession of the United States with respect to income effectively connected with the conduct of a trade or business within the United States.

(b) Special rules. --

(1) For purposes of subsection (a) and for purposes of determining the deductions allowable under sections 873(a) and 882(c), in determining the amount of any tax paid or accrued to any foreign country or possession there shall not be taken into account any amount of tax to the extent the tax so paid or accrued is imposed with respect to income from sources within the United States which would not be taxed by such foreign country or possession but for the fact that --

(A) in the case of a nonresident alien individual, such individual is a citizen or resident of such foreign country or possession, or

(B) in the case of a foreign corporation, such corporation was created or organized under the law of such foreign country or possession or is domiciled for tax purposes in such country or possession.

(2) For purposes of subsection (a), in applying section 904 the taxpayer's taxable income shall be treated as consisting only of the taxable income effectively connected with the taxpayer's conduct of a trade or business within the United States.

(3) The credit allowed pursuant to subsection (a) shall not be allowed against any tax imposed by section 871(a) (relating to income of nonresident alien individual not connected with United States business) or 881 (relating to income of foreign corporations not connected with United States business).

(4) For purposes of sections 902(a) and 78, a foreign corporation choosing the benefits of this subpart which receives dividends shall, with respect to such dividends, be treated as a domestic corporation.

(5) No credit shall be allowed under this section for any income, war profits and excess profits taxes paid or accrued with respect to the foreign trade income (within the meaning of section 923(b)) of a FSC.

(6) For purposes of section 902, any income, war profits, and excess profits taxes paid or accrued (or deemed paid or accrued) to any foreign country or possession of the United States with respect to income effectively connected with the conduct of a trade or business within the United States shall not be taken into account, and any accumulated profits attributable to such income shall not be taken into account.

(7) No credit shall be allowed under this section against the tax imposed by section 884.

907. Special rules in case of foreign oil and gas income

(a) Reduction in amount allowed as foreign tax under section 901. -- In applying section 901, the amount of any oil and gas extraction taxes paid or accrued (or deemed to have been paid) during the taxable year which would (but for this subsection) be taken into account for purposes of section 901 shall be reduced by the amount (if any) by which the amount of such taxes exceeds the product of --

(1) the amount of the foreign oil and gas extraction income for the taxable year,

(2) multiplied by --

(A) in the case of a corporation, the percentage which is equal to the highest rate of tax specified under section 11(b), or

(B) in the case of an individual, a fraction the numerator of which is the tax against which the credit under section 901 (a) is taken and the denominator of which is the taxpayer's entire taxable income.

(b) Foreign taxes on foreign oil related income. -- For purposes of this subtitle, in the case of taxes paid or accrued to any foreign country with respect to foreign oil, related income, the term "income, war profits, and excess profits taxes" shall not include any amount paid or accrued after December 31, 1982, to the extent that the Secretary determines that the foreign law imposing such amount of tax is structured, or in fact operate, so that the amount of tax imposed with respect to foreign oil related income will generally be materially greater, over a reasonable period of time, than the amount generally imposed on income that is neither foreign oil related income nor foreign oil and gas extraction income. In computing the amount not treated as tax under this subsection, such amount shall be treated as a deduction under the foreign law.

(c) Foreign income definitions and special rules. -- For purposes of this section --

(1) Foreign oil and gas extraction income. -- The term "foreign oil and gas extraction income" means the taxable income derived from sources without the United States and its possessions from --

(A) the extraction (by the taxpayer or any other person) of minerals from oil or gas wells, or

(B) the sale or exchange of assets used by the taxpayer in the trade or business described in subparagraph (A).

(2) Foreign oil related income. -- The term "foreign oil related income" means the taxable income derived from sources outside the United States and its possessions from --

(A) the processing of minerals extracted (by the taxpayer or by any other person) from oil or gas wells into their primary products,

(B) the transportation of such minerals or primary products,

(C) the distribution or sale of such minerals or primary products,

(D) the disposition of assets used by the taxpayer in the trade or business described in subparagraph (A), (B), or (C), or

(E) the performance of any other related service.

(3) Dividends, interest, partnership distribution, etc. --  
The term "foreign oil and gas extraction income" and the term  
"foreign oil related income" include --

(A) dividends and interest from a foreign corporation in  
respect of which taxes are deemed paid by the taxpayer under  
section 902,

(B) amounts with respect to which taxes are deemed paid  
under section 960(a), and

(C) the taxpayer's distributive share of the income of  
partnerships.

to the extent such dividends, interest, amounts, or distributive  
share is attributable to foreign oil and gas extraction income,  
or to foreign oil related incomes, as the case may be; except  
that interest described in subparagraph (A) shall not be taken  
into account in computing foreign oil and gas extraction income  
but shall be taken into account in computing foreign oil-related  
income.

(4) Recapture of foreign oil and gas extraction losses by  
recharacterizing later extraction income. --

(A) In general. -- That portion of the income of the  
taxpayer for the taxable year which (but for this paragraph)  
would be treated as foreign oil and gas extraction income shall be  
treated as income (from sources without the United States) which  
is not foreign oil and gas extraction income to the extent of the  
excess of --

(i) the aggregate amount of foreign oil extraction losses  
for preceding taxable years beginning after December 31, 1982,  
over

(ii) so much of such aggregate amount as was recharacterized  
under this subparagraph for preceding taxable years beginning  
after December 31, 1982.

(B) Foreign oil extraction loss defined. --

(i) In general. -- For purposes of this paragraph, the  
term "foreign oil extraction loss" means the amount by which --

(I) the gross income for the taxable year from sources  
without the United States and its possessions (whether or not the  
taxpayer chooses the benefits of this subpart for such taxable  
year) taken into account in determining the foreign oil and gas  
extraction income for such year, is exceeded by

(II) the sum of the deductions properly apportioned or  
allocated thereto.

(ii) Net operating loss deduction not taken into account. --  
For purposes of clause (i), the net operating loss deduction  
allowable for the taxable year under section 172(a) shall not be  
taken into account.

(iii) Expropriation and casualty losses not taken into  
account. --

For purposes of clause (i), there shall not be taken into  
account --

(I) any foreign expropriation loss (as defined in section  
172(h)) for the taxable year, or

(II) any loss for the taxable year which arises from fire,  
storm, shipwreck, or other casualty, or from theft,  
to the extent such loss is not compensated for by insurance or  
otherwise.

(5) Oil and gas extraction taxes. -- The term "oil and gas extraction taxes" means any income, war profits, and excess profits taxes" means any income, war profits, and excess profits tax paid or accrued (or deemed to have been paid under section 902 or 960) during the taxable year with respect to foreign oil and gas extraction income (determined without regard to paragraph (4)) or loss which would be taken into account for purposes of section 901 without regard to this section.

(d) Disregard of certain posted prices, etc. -- For purposes of this chapter, in determining the amount of taxable income in the case of foreign oil and gas extraction income, if the oil or gas is disposed of, or is acquired other than from the government of a foreign country, at a posted price (or other pricing arrangement) which differs from the fair market value for such oil or gas, such fair market value shall be used in lieu of such posted price (or other pricing arrangement).

(e) Repealed.

(f) Carryback and carryover of disallowed credits. --

(1) In general. -- If the amount of the oil and gas extraction taxes paid or accrued during any taxable year exceeds the limitation provided by subsection (a) for such taxable year (hereinafter in this subsection referred to as the "unused credit year"), such excess shall be deemed to be oil and gas extraction taxes paid or accrued in the second preceding taxable year, in the first preceding taxable year, and in the first, second, third, fourth, or fifth succeeding taxable year, in that order and to the extent not deemed tax paid or accrued in a prior taxable year by reason of the limitation imposed by paragraph (2). Such amount deemed paid or accrued in any taxable year may be availed of only as a tax credit and not as a deduction and only if the taxpayer for such year chooses to have the benefits of this subpart as to taxes paid or accrued for that year to foreign countries or possessions. For purposes of this subsection, the terms "second preceding taxable year", and "first preceding taxable year" do not include any taxable year ending before January 1, 1975.

(2) Limitation. -- The amount of the unused oil and gas extraction taxes which under paragraph (1) may be deemed paid or accrued in any preceding or succeeding taxable year shall not exceed the lesser of --

(A) the amount by which the limitation provided by subsection (a) for such taxable year exceeds the sum of --

(i) the oil and gas extraction taxes paid or accrued during such taxable year, plus

(ii) the amounts of the oil and gas extraction taxes which by reason of this subsection are deemed paid or accrued in such taxable year and are attributable to taxable years preceding the unused credit year; or

(B) the amount by which the limitation provided by section 904 for such taxable year exceeds the sum of --

(i) the taxes paid or accrued (or deemed to have been paid under section 902 or 960) to all foreign countries and possessions of the United States during such taxable year,

(ii) the amount of such taxes which were deemed paid or accrued in such taxable year under section 904(c) and which are

attributable to taxable years preceding the unused credit year,  
plus

(iii) the amount of the oil and gas extraction taxes which  
by reason of this subsection are deemed paid or accrued in such  
taxable year and are attributable to taxable years preceding the  
unused credit year.

(3) Special rules. --

(A) In the case of any taxable year which is an unused  
credit year under this subsection and which is an unused credit  
year under section 904(c), the provisions of this subsection shall  
be applied before section 904(c).

(B) For purposes of determining the amount of taxes paid or  
accrued in any taxable year which may be deemed paid or accrued  
in a preceding or succeeding taxable year under section 904(c),  
any tax deemed paid or accrued in such preceding or succeeding  
taxable year under this subsection shall be considered to be tax  
paid or accrued in such preceding or succeeding taxable year.

(C) Repealed.

908. Reduction of credit for participation in or cooperation with  
an international boycott

(a) In general. -- If a person, or a member of a  
controlled group (within the meaning of section 993(a)(3)) which  
includes such person, participates in or cooperates with an  
international boycott during the taxable year (within the meaning  
of section 999(b)), the amount of the credit allowable under  
section 901 to such person, or under section 902 or 960 to United  
States shareholders of such person, for foreign taxes paid during  
the taxable year shall be reduced by an amount equal to the  
product of --

(1) the amount of the credit which, but for this section,  
would be allowed under section 901 for the taxable year,  
multiplied by

(2) the international boycott factor (determined under  
section 999).

(b) Application with sections 275(a)(4) and 78. -- Section  
275(a)(4) and section 78 shall not apply to any amount of taxes  
denied credit under subsection (a).

911. Citizens or residents of the United States living abroad

(a) Exclusion from gross income. -- At the election of a  
qualified individual (made separately with respect to paragraphs  
(1) and (2)), there shall be excluded from the gross income of  
such individual, and exempt from taxation under this subtitle,  
for any taxable year --

(1) the foreign earned income of such individual, and

(2) the housing cost amount  
of such individual.

(b) Foreign earned income. --

(1) Definitions. -- For purposes of this section --

(A) In general. -- The term "foreign earned income" with  
respect to any individual means the amount received by such  
individual from sources within a foreign country or countries  
which constitute earned income attributable to services performed

by such individual during the period described in subparagraph (A) or (B) of subsection (d)(1), whichever is applicable.

(B) Certain amounts not included in foreign earned income.

-- The foreign earned income for an individual shall not include amounts --

(i) received as a pension or annuity,

(ii) paid by the United States or an agency thereof to an employee of the United States or an agency thereof,

(iii) included in gross income by reason of section 402(b) (relating to taxability of beneficiary on non-exempt trust) or section 403(c) (relating to taxability of beneficiary under a nonqualified annuity), or

(iv) received after the close of the taxable year following the taxable year in which the services to which the amounts are attributable are performed.

(2) Limitation on foreign earned income. --

(A) In general. -- The foreign earned income of an individual which may be excluded under subsection (a)(1) for any taxable year shall not exceed the amount of foreign earned income computed on a daily basis at an annual rate of \$70,000.

(B) Attribution to year in which services are performed. --

- For purposes of applying subparagraph (A), amounts received shall be considered received in the taxable year in which the services to which the amounts are attributable are performed.

(C) Treatment of community income. -- In applying subparagraph (A) with respect to amounts received from services performed by a husband or wife which are community income under community property laws applicable to such income, the aggregate amount which may be excludable from the gross income of such husband and wife under subsection (a)(1) for any taxable year shall equal the amount which would be so excludable if such amounts did not constitute community income.

(c) Housing cost amount. -- For purposes of this section --

(1) In general. -- The term "housing cost amount" means an amount equal to the excess of --

(A) the housing expenses of an individual for the taxable year, over

(B) an amount equal to the product of --

(1) 16 percent of the salary (computed on a daily basis) of an employee of the United States who is compensated at a rate equal to the annual rate paid for step 1 of grade GS-14, multiplied by

(ii) the number of days of such taxable year within the applicable period described in subparagraph (A) or (B) of subsection (d)(1).

(2) Housing expenses. --

(A) In general. -- The term "housing expenses" means the reasonable expenses paid or incurred during the taxable year by or on behalf of an individual for housing for the individual (and, if they reside with him, for his spouse and dependents) in a foreign country. The term --

(i) includes expenses attributable to the housing (such as utilities and insurance), but

(ii) does not include interest and taxes of the kind deductible under section 163 or 164 or any amount allowable as a deduction under section 216(a).

Housing expenses shall not be treated as reasonable to the extent such expenses are lavish or extravagant under the circumstances.

(B) Second foreign household. --

(i) In general. -- Except as provided in clause (ii), only housing expenses incurred with respect to that abode which bears the closest relationship to the tax home of the individual shall be taken into account under paragraph (1).

(ii) Separate household for spouse and dependents. -- If an individual maintains a separate abode outside the United States for his spouse and dependents and they do not reside with him because of living conditions which are dangerous, unhealthful, or otherwise adverse, then --

(I) the words "if they reside with him" in subparagraph (A) shall be disregarded, and

(II) the housing expenses incurred with respect to such abode shall be taken into account under paragraph (1).

(3) Special rules where housing expenses not provided by employer. --

(A) In general. -- To the extent the housing cost amount of any individual for any taxable year is not attributable to employer provided amounts, such amount shall be treated as a deduction allowable in computing adjusted gross income to the extent of the limitation of subparagraph (B).

(B) Limitation. -- For purposes of subparagraph (A), the limitation of this subparagraph is the excess of --

(i) the foreign earned income of the individual for the taxable year, over

(ii) the amount of such income excluded from gross income under subsection (a) for the taxable year.

(C) 1-year carryover of housing amounts not allowed by reason of subparagraph (B). --

(i) In general. -- The amount not allowable as a deduction for any taxable year under subparagraph (A) by reason of the limitation of subparagraph (B) shall be treated as a deduction allowable in computing adjusted gross income for the succeeding taxable year (and only for the succeeding taxable year) to the extent of the limitation of clause (ii) for such succeeding taxable year.

(ii) Limitation. -- For purposes of clause (i), the limitation of this clause for any taxable year is the excess of --

(I) the limitation of subparagraph (B) for such taxable year, over

(II) amounts treated as a deduction under subparagraph (A) for such taxable year.

(D) Employer provided amounts. -- For purposes of this paragraph, the term "employer provided amounts" means any amount paid or incurred on behalf of the individual by the individual's employer which is foreign earned income included in the individual's gross income for the taxable year (without regard to this section).



(E) Foreign earned income. -- For purposes of this paragraph, an individual's foreign earned income for any taxable year shall be determined without regard to the limitation of subparagraph (A) of subsection (b)(2).

(d) Definitions and special rules. -- For purposes of this section --

(1) Qualified individual. -- The term "qualified individual" means an individual whose tax home is in a foreign country and who is --

(A) a citizen of the United States and establishes to the satisfaction of the Secretary that he has been a bona fide resident of a foreign country or countries for an uninterrupted period which includes an entire taxable year, or

(B) a citizen or resident of the United States and who, during any period of 12 consecutive months, is present in a foreign country or countries during at least 330 full days in such period.

(2) Earned income. --

(A) In general. -- The term "earned income" means wages, salaries, or professional fees, and other amounts received as compensation for personal services actually rendered, but does not include that part of the compensation derived by the taxpayer for personal services rendered by him to a corporation which represents a distribution of earnings or profits rather than a reasonable allowance as compensation for the personal services actually rendered.

(B) Taxpayer engaged in trade or business. -- In the case of a taxpayer engaged in a trade or business in which both personal services and capital are material income-producing factors, under regulations prescribed by the Secretary, a reasonable allowance as compensation for the personal services rendered by the taxpayer, not in excess of 30 percent of his share of the net profits of such trade or business, shall be considered as earned income.

(3) Tax home. -- The term "tax home" means, with respect to any individual, such individual's home for purposes of section 162(a)(2) (relating to traveling expenses while away from home). An individual shall not be treated as having a tax home in a foreign country for any period for which his abode is within the United States.

(4) Waiver of period of stay in foreign country. -- Notwithstanding paragraph (1), an individual who --

(A) is a bona fide resident of, or is present in, a foreign country for any period.

(B) leaves such foreign country after August 31, 1978 --

(i) during any period during which the Secretary determines, after consultation with the Secretary of State or his delegate, that individuals were required to leave such foreign country because of war, civil unrest, or similar adverse conditions in such foreign country which precluded the normal conduct of business by such individuals, and

(ii) before meeting the requirements of such paragraph (1), and

(C) establishes to the satisfaction of the Secretary that such individual could reasonably have been expected to have met

such requirements but for the conditions referred to in clause (i) of subparagraph (B), shall be treated as a qualified individual with respect to the period described in subparagraph (A) during which he was a bona fide resident of, or was present in, the foreign country, and in applying subsections (b)(2)(A) and (c)(1)(B)(ii) with respect to such individual, only the days within such period shall be taken into account.

(5) Test of bona fide residence. -- If --

(A) an individual who has earned income from sources within a foreign country submits a statement to the authorities of that country that he is not a resident of that country, and

(B) such individual is held not subject as a resident of that country to the income tax of that country by its authorities with respect to such earnings, then such individual shall not be considered a bona fide resident of that country for purposes of paragraph (1)(A).

(6) Denial of double benefits. -- No deduction or exclusion from gross income under this subtitle or credit against the tax imposed by this chapter (including any credit or deduction for the amount of taxes paid or accrued to a foreign country or possession of the United States) shall be allowed to the extent such deduction, exclusion, or credit is properly allocable to or chargeable against amounts excluded from gross income under subsection (a).

(7) Aggregate benefit cannot exceed foreign earned income. -- The sum of the amount excluded under subsection (a) and the amount deducted under subsection (c)(3)(A) for the taxable year shall not exceed the individual's foreign earned income for such year.

(8) Limitation on income earned in restricted country. --

(A) In general. -- If travel (or any transaction in connection with such travel) with respect to any foreign country is subject to the regulations described in subparagraph (B) during any period--

(i) the term "foreign earned income" shall not include any income from sources within such country attributable to services performed during such period,

(ii) the term "housing expenses" shall not include any expenses allocable to such period for housing in such country or for housing of the spouse or dependents of the taxpayer in another country while the taxpayer is present in such country, and

(iii) an individual shall not be treated as a bona fide resident of, or as present in, a foreign country for any day during which such individual was present in such country during such period.

(B) Regulations. -- For purposes of this paragraph, regulations are described in this subparagraph if such regulations --

(i) have been adopted pursuant to the Trading With the Enemy Act (50 U.S.C. App. 1 et seq.), or the International Emergency Economic Powers Act (50 U.S.C. 1701 et seq.), and

(ii) include provisions generally prohibiting citizens and

residents of the United States from engaging in transactions related to travel to, from, or within a foreign country.

(C) Exception. -- Subparagraph (A) shall not apply to any individual during any period in which such individual's activities are not in violation of the regulations described in subparagraph (B).

(9) Regulations. -- The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this section, including regulations providing rules -

(A) for cases where a husband and wife each have earned income from sources outside the United States, and

(B) for married individuals filing separate returns.

(e) Election. --

(1) In general. -- An election under subsection (a) shall apply to the taxable year for which made and to all subsequent taxable years unless revoked under paragraph (2).

(2) Revocation. -- A taxpayer may revoke an election made under paragraph (1) for any taxable year after the taxable year for which such election was made. Except with the consent of the Secretary, any taxpayer who makes such a revocation for any taxable year may not make another election under this section for any subsequent taxable year before the 6th taxable year after the taxable year for which such revocation was made.

(f) Cross references. --

For administrative and penal provisions relating to the exclusions provided for in this section, see sections 6001, 6011, 6012(c), and the other provisions of subtitle F.

## 912. Exemption 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) chapter 9 of title I of the Foreign Service Act of 1980,

(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 (or in the case of judicial officers or employees of the United States, in accordance with rules similar to such regulations).

(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.

913. Repealed.

921. Exempt foreign trade income excluded from gross income

(a) Exclusion. -- Exempt foreign trade income of a FSC shall be treated as foreign source income which is not effectively connected with the conduct of a trade or business within the United States.

(b) Proportionate allocation of deductions to exempt foreign trade income. -- Any deductions of the FSC properly apportioned and allocated to the foreign trade income derived by a FSC from any transaction shall be allocated between --

- (1) the exempt foreign trade income derived from such transaction, and
- (2) the foreign trade income (other than exempt foreign trade income) derived from such transactions, on a proportionate basis.

(c) Denial of credits. -- Notwithstanding any other provision of this chapter, no credit (other than a credit allowable under section 27(a), 33, or 34) shall be allowed under this chapter to any FSC.

(d) Foreign trade income, investment income, and carrying charges treated as effectively connected with United States business. -- For purposes of this chapter --

- (1) all foreign trade income of a FSC other than --
  - (A) exempt foreign trade income, and
  - (B) section 923(a)(2) non-exempt income,
- (2) all interest, dividends, royalties, and other investment income received or accrued by a FSC, and
- (3) all carrying charges received or accrued by a FSC, shall be treated as income effectively connected with a trade or business conducted through a permanent establishment of such corporation within the United States. Income described in paragraph (1) shall be treated as derived from sources within the United States.

922. FSC defined

(a) FSC defined. -- For purposes of this title, the term "FSC" means any corporation --

- (1) which --
  - (A) was created or organized --

(i) under the laws of any foreign country which meets the requirements of section 927(e)(3), or

(ii) under the laws applicable to any possession of the United States,

(B) has no more than 25 shareholders at any time during the taxable year,

(C) does not have any preferred stock outstanding at any time during the taxable year.

(D) during the taxable year --

(i) maintains an office located outside the United States in a foreign country which meets the requirements of section 927(e)(3) or in any possession of the United States,

(ii) maintains a set of the permanent books of account (including invoices) of such corporation at such office, and

(iii) maintains at a location within the United States the records which such corporation is required to keep under section 6001,

(E) at all times during the taxable year, has a board of directors which includes at least one individual who is not a resident of the United States, and

(F) is not a member, at any time during the taxable year, of any controlled group of corporations of which a DISC is a member, and

(2) which has made an election (at the time and in the manner provided in section 927(f)(1)) which is in effect for the taxable year to be treated as a FSC.

(b) Small FSC defined. -- For purposes of this title, a FSC is a small FSC with respect to any taxable year if --

(1) such corporation has made an election (at the time and in the manner provided in section 927(f)(1)) which is in effect for the taxable year to be treated as a small FSC, and

(2) such corporation is not a member, at any time during the taxable year, of a controlled group of corporations which includes a FSC unless such other FSC has also made an election under paragraph (1) which is in effect for such year.

### 923. Exempt foreign trade income

(a) Exempt foreign trade income. -- For purposes of this subpart --

(1) In general. -- The term "exempt foreign trade income" means the aggregate amount of all foreign trade income of a FSC for the taxable year which is described in paragraph (2) or (3).

(2) Income determined without regard to administrative pricing rules. -- In the case of any transaction to which paragraph (3) does not apply, 43 percent of the foreign trade income derived from such transaction shall be treated as described in this paragraph. For purposes of the preceding sentence, foreign trade income shall not include any income property allocable to excluded property described in subparagraph (B) of section 927(a)(2) (relating to intangibles).

(3) Income determined with regard to administrative pricing rules. -- In the case of any transaction with respect to which paragraph (1) or (2) of section 925(a) (or the corresponding provisions of the regulations prescribed under section 925(b))

applies, 16/23 of the foreign trade income derived from such transaction shall be treated as described in this paragraph.

(4) Special rule for foreign trade income allocable to a cooperative. --

(A) In general. -- In any case in which a qualified cooperative is a shareholder of a FSC, paragraph (3) shall be applied with respect to that portion of the foreign trade income of such FSC for any taxable year which is properly allocable to the marketing of agricultural or horticultural products (or the providing of related services) by such cooperative by substituting "100 percent" for "16/23".

(B) Paragraph only to apply to amounts FSC distributes. -- Subparagraph (A) shall not apply for any taxable year unless the FSC distributes to the qualified cooperative the amount which (but for such subparagraph) would not be treated as exempt foreign trade income. Any distribution under this subparagraph for any taxable year --

(i) shall be made before the due date for filing the return of tax for such taxable year, but

(ii) shall be treated as made on the last day of such taxable year.

(5) Special rule for military property. -- Under regulations prescribed by the Secretary, that portion of the foreign trading gross receipts of the FSC for the taxable year attributable to the disposition of, or services relating to, military property (within the meaning of section 995(b)(3)(B)) which may be treated as exempt foreign trade income shall equal 50 percent of the amount which (but for this paragraph) would be treated as exempt foreign trade income.

(6) Cross reference. --

For reduction in amount of exempt foreign trade income, see section 291(a)(4).

(b) Foreign trade income defined. -- For purposes of this subpart, the term "foreign trade income" means the gross income of a FSC attributable to foreign trading gross receipts.