

924. Foreign trading gross receipts

(a) In general. -- Except as otherwise provided in this section, for purposes of this subpart, the term "foreign trading gross receipts" means the gross receipts of any FSC which are --

- (1) from the sale, exchange, or other disposition of export property,
- (2) from the lease or rental of export property for use by the lessee outside the United States,
- (3) for services which are related and subsidiary to --
 - (A) any sale, exchange, or other disposition of export property by such corporation, or
 - (B) any lease or rental of export property described in paragraph (2) by such corporation,
- (4) for engineering or architectural services for construction projects located (or proposed for location) outside the United States, or
- (5) for the performance of managerial services for an unrelated FSC or DISC in furtherance of the production of foreign trading gross receipts described in paragraph (1), (2), or (3).

Paragraph (5) shall not apply to a FSC for any taxable year unless at least 50 percent of its gross receipts for such taxable year is derived from activities described in paragraph (1), (2), or (3).

(b) Foreign management and foreign economic process requirements.

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- (1) In general. -- Except as provided in paragraph (2) --
 - (A) a FSC shall be treated as having foreign trading gross receipts for the taxable year only if the management of such corporation during such taxable year takes place outside the United States as required by subsection (c), and
 - (B) a FSC has foreign trading gross receipts from any transaction only if economic processes with respect to such transaction take place outside the United States as required by subsection (d).
- (2) Exception for small FSC. --
 - (A) In general. -- Paragraph (1) shall not apply with respect to any small FSC.
 - (B) Limitation on amount of foreign trading gross receipts of small FSC taken into account. --
 - (i) In general. -- Any foreign trading gross receipts of a small FSC for the taxable year which exceed \$5,000,000 shall not be taken into account in determining the exempt foreign trade income of such corporation and shall not be taken into account under any other provision of this subpart.
 - (ii) Allocation of limitation. -- If the foreign trading gross receipts of a small FSC exceed the limitation of clause (i), the corporation may allocate such limitation among such gross receipts in such manner as it may select (at such time and in such manner as may be prescribed in regulations).
 - (iii) Receipts of controlled group aggregated. -- For purposes of applying clauses (i) and (ii), all small FSC's which are members of the same controlled group of corporations shall be treated as a single corporation.
 - (iv) Allocation of limitation among members of controlled group. -- The limitation under clause (i) shall be allocated among the foreign trading gross receipts of

small FSC's which are members of the same controlled group of corporations in a manner provided in regulations prescribed by the Secretary.

(c) Requirement that FSC be managed outside the United States. --

The management of a FSC meets the requirements of this subsection for the taxable year if --

(1) all meetings of the board of directors of the corporation, and all

meetings of the shareholders of all corporation, are outside the United States,

(2) the principal bank account of the corporation is maintained in a

foreign country which meets the requirements of section 927(e)(3) or in a possession of the United States at all times during the taxable year, and

(3) all dividends, legal and accounting fees, and salaries of officers

and members of the board of directors of the corporation disbursed during the taxable year are disbursed out of bank accounts of the corporation maintained outside the United States.

(d) Requirements that economic processes take place outside the

United States. --

(1) In general. -- The requirements of this subsection are met with

respect to the gross receipts of a FSC derived from an transaction if --

(A) such corporation (or any person acting under a contract with such

corporation) has participated outside the United States in the solicitation (other than advertising), the negotiation, or the making of the contract relating to such transaction, and

(B) the foreign direct costs incurred by the FSC attributable to the

transaction equal or exceed 50 percent of the total direct cost attributable to the transaction.

(2) Alternative 85-percent test. -- A corporation shall be treated as

satisfying the requirements of paragraph (1)(B) with respect to any transaction if, with respect to each of at least 2 paragraphs of subsection (e), the foreign direct costs incurred by such

corporation attributable to activities described in such paragraph equal or exceed 85 percent of the total direct costs attributable to activities described in such paragraph.

(3) Definitions. -- For purposes of this subsection --

(A) Total direct costs. -- The term "total direct costs" means, with

respect to any transaction, the total direct costs incurred by the FSC attributable to activities described in subsection (e) performed at any location by the FSC or any person acting under a contract with such FSC.

(B) Foreign direct costs. -- The term "foreign direct costs" means, with

respect to any transaciton, the portion of the total direct costs which are attributable to activities performed outside the United States.

(4) Rules for commissions, etc. -- The Secretary shall prescribe such

regulations as may be necessary to carry out the purposes of this subsection and subsection (e) in the case of commissions, rentals, and furnishing of services.

(e) Activities relating to disposition of export property. -- The

activities referred to in subsection (d) are --

(1) advertising and sales promotion,

(2) the processing of customer orders and the arranging for delivery of

the export property,

(3) transportation from the time of acquisition by the FSC (or, in the case of a commission relationship, from the beginning of such relationship for such transaction) to the delivery to the customer.

(4) the determination and transmittal of a final invoice or statement of

account and the receipt of payment, and

(5) the assumption of credit risk.

(f) Certain receipts not included in foreign trading gross receipts. --

(1) Certain receipts excluded on basis of use; subsidized receipts and receipts from related parties excluded. -- The term "foreign trading gross receipts" shall not include receipts of a FSC from a transaction if --

(A) the export property or services --

(i) are for ultimate use in the United States, or

(ii) are for use by the United States or any instrumentality thereof and such use of export property or services is required by law or regulation.

(B) such transaction is accomplished by a subsidy granted by the United States or any instrumentality thereof, or services is required by law or regulation.

(C) such receipts are from another FSC which is a member of the same controlled group of corporations of which such corporation is a member.

In the case of gross receipts of a FSC from a transaction involving any property, subparagraph (C) shall not apply if such FSC (and all other FSC's which are members of the same controlled group and which receive gross receipts from a transaction involving such property) do not use the pricing rules under paragraph (1) of section 925(a) (or the corresponding provisions of the regulations prescribed under section 925(b)) with respect to any transaction involving such property.

(2) Investment income; carrying charges. -- The term "foreign trading gross receipts" shall not include any investment income or carrying charges.

925. Transfer pricing rules

(a) In general. -- In the case of a sale of export property to a FSC by a person described in section 482, the taxable income of such FSC and such person shall be based upon a transfer price which would allow such FSC to derive taxable income attributable to such sale (regardless of the sales price actually charged) in an amount which does not exceed the greatest of --

(1) 1.83 percent of the foreign trading gross receipts derived from the sale of such property by such FSC,

(2) 23 percent of the combined taxable income of such FSC and such person which is attributable to the foreign trading gross receipts derived from the sale of such property by such FSC, or

(3) taxable income based upon the sale price actually charged (but subject to the rules provided in section 482).

Paragraphs (1) and (2) shall apply only if the FSC meets the requirements of subsection (c) with respect to the sale.

(b) Rules for commissions, rentals, and marginal costing. -- The Secretary shall prescribe regulations setting forth --

(1) rules which are consistent with the rules set forth in subsection (a) for the application of this section in the case of commissions, rentals, and other income, and

(2) rules for the allocation of expenditures in computing combined taxable income under subsection (a)(2) in those cases where a FSC is seeking to establish or maintain a market for export property.

(c) Requirements for use of administrative pricing rules. -- A sale by

a FSC meets the requirements of this subsection if--

- (1) all of the activities described in section 924(e) attributable to such sale, and
- (2) all of the activities relating to the solicitation (other than advertising), negotiation, and making of the contract for such sale, have been performed by such FSC (or by another person acting under a contract with such FSC).
- (d) Limitation on gross receipts pricing rule. -- The amount determined under subsection (a)(1) with respect to any transaction shall not exceed 2 times the amount which would be determined under subsection (a)(2) with respect to such transaction.
- (e) Taxable income. -- For purposes of this section, the taxable income of a FSC shall be determined without regard to section 921.
- (f) Special rule for cooperatives. -- In any case in which a qualified cooperative sells export property to a FSC, in computing the combined taxable income of such FSC and such organization for purposes of subsection (a)(2), there shall not be taken into account any deduction allowable under subsection (b) or (c) of section 1.382 (relating to patronage dividends, per-unit retain allocations, and nonpatronage distributions).

926. Distributions to shareholders

(a) Distributions made first out of foreign trade income. -- For purposes of this title, any distribution to a shareholder of a FSC by such FSC which is made out of earnings and profits shall be treated as made --

(1) first, out of earnings and profits attributable to foreign trade income, to the extent thereof, and

(2) then, out of any other earnings and profits.

(b) Distributions by FSC to nonresident aliens and foreign corporations treated as United States connected. -- For purposes of this title, any distribution by a FSC which is made out of earnings and profits attributable to foreign trade income to any shareholder of such corporation which is a foreign corporation or a nonresident alien individual shall be treated as a distribution --

(1) which is effectively connected with the conduct of a trade or business conducted through a permanent establishment of such shareholder within the United States, and

(2) of income which is derived from sources within the United States.

(c) FSC includes former FSC. -- For purposes of this section, the term "FSC" includes a former FSC.

927. Other definitions and special rules

(a) Export property. -- For purposes of this subpart --

(1) In general. -- The term "export property" means property --

(A) manufactured, produced, grown, or extracted in the United States by a person other than a FSC,

(B) held primarily for sale, lease, or rental, in the ordinary course of trade or business, by, or to, a FSC, for direct use, consumption, or disposition outside the United States, and

(C) not more than 50 percent of the fair market value of which is attributable to articles imported into the United States.

For purposes of subparagraph (C), the fair market value of any article imported into the United States shall be its appraised value, as determined by the Secretary under section 402 of the Tariff Act of 1930 (19 U.S.C. 1401(a)) in connection with its importation.

(2) Excluded property. -- The term "export property" shall not include

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(A) property leased or rented by a FSC for use by any member of a controlled group of corporations of which such FSC is a member,

(B) patents, inventions, models, designs, formulas, or processes whether or not patented, copyrights (other than films, tapes, records, or similar reproductions, for commercial or home use), good will, trademarks, trade brands, franchises, or other like property,

(C) oil or gas (or any primary product thereof), or

(D) products the export of which is prohibited or curtailed to effectuate the policy set forth in paragraph (2)(C) of section 3 of the Export Administration Act of 1979 (relating to the protection of the domestic economy).

(3) Property in short supply. -- If the President determines that the supply of any property described in paragraph (1) is insufficient to meet the requirements of the domestic economy, he may by Executive order designate the property as in short supply. Any property so designated shall not be treated as export property during the period beginning with the date specified in the Executive order and ending with the date specified in an Executive order setting forth the President's determination that the property is no longer in short supply.

(4) Qualified cooperative. -- The term "qualified cooperative" means any organization to which part I of subchapter T applies which is engaged in the marketing of agricultural or horticultural products.

(b) Gross receipts. --

(1) In general. -- For purposes of this subpart, the term "gross receipts" means --

(A) the total receipts from the sale, lease, or rental of property held primarily for sale, lease, or rental in the ordinary course of trade or business, and

(B) gross income from all other sources.

(2) Gross receipts taken into account in case of commissions. -- In the case of commissions on the sale, lease, or rental of property, the amount taken into account for purposes of this subpart as gross receipts shall be the gross receipts on the sale, lease, or rental of the property on which such commissions arose.

(c) Investment income. -- For purposes of this subpart, the term "investment income" means --

(1) dividends,

(2) interest,

(3) royalties,

(4) annuities,

(5) rents (other than rents from the lease or rental of export property for use by the lessee outside of the United States),

(6) gains from the sale or exchange of stock or securities,

(7) gains from futures transactions in any commodity on, or subject to the rules of, a board of trade or commodity exchange (other than gains which arise out of a bona fide hedging transaction entered into by the FSC in the manner in which such business is customarily conducted by others),

(8) amounts includible in computing the taxable income of the corporation under part I of subchapter J, and

(9) gains from the sale or other disposition of any interest in an estate or trust.

(d) Other definitions. -- For purposes of this subpart --

(1) Carrying charges. -- The term "transaction" means --

(A) carrying charges, and

(B) under regulations prescribed by the Secretary, any amount in excess of the price for an immediate cash sale and any other unstated interest,

(2) Transaction. --

(A) In general. -- The term "transaction" means --

(i) any sale, exchange, or other disposition,

(ii) any lease or rental, and

(iii) any furnishing of services.

(B) Grouping of transactions. -- To the extent provided in regulations, any provision of this subpart which, but for this subparagraph, would be applied on a transaction-by-transaction basis may be applied by the taxpayer on the basis of groups of transactions based on product lines or recognized industry or trade usage. Such regulations may permit different groupings for different purposes.

(3) United States defined. -- The term "United States" includes the Commonwealth of Puerto Rico.

(4) Controlled group of corporations. -- The term "controlled group of corporations" has the meaning given to such term by section 1563(a), except that --

(A) "more than 50 percent" shall be substituted for "at least 80 percent" each place it appears therein, and

(B) section 1563(b) shall not apply.

(5) Possessions. -- The term "possession of the United States" means Guam, American Samoa, the Commonwealth of the Northern Mariana Islands, and the Virgin Islands of the United States.

(6) Section 923(a)(2) non-exempt income. -- The term "section 923(a)(2) non-exempt income" means any foreign trade income from a transaction with respect to which paragraph (1) or (2) of section 925(a) does not apply and which is not exempt foreign trade income. Such term shall not include any income which is effectively connected with the conduct of a trade or business within the United States (determined without regard to this subpart).

(e) Special rules. --

(1) Source rules for related persons. -- Under regulations, the income of a person described in section 482 from a transaction giving rise to foreign trading gross receipts of a FSC which is treated as from sources outside the United States shall not exceed the amount which would be treated as foreign source income earned by such person if the pricing rule under section 994 which corresponds to the rule used under section 925 with respect to such transaction applied to such transaction.

(2) Participation in international boycotts, etc. -- Under regulations prescribed by the Secretary, the exempt foreign trade income of a FSC for any taxable year shall be limited under rules similar to the rules of clauses (ii) and (iii) of section 995(b)(1)(F).

(3) Exchange of information requirements. -- For purposes of this title,

the term "FSC" shall not include any corporation which was created or organized under the laws of any foreign country unless there is in effect between such country and the United States --

(A) a bilateral or multilateral agreement described in section 274(h)(6)

(C) (determined by treating any reference to a beneficiary country and by applying such section without regard to clause (ii) thereof), or

(B) an income tax treaty which contains an exchange of information program --

(i) which the Secretary certifies (and has not revoked such certification) is satisfactory in practice for purposes of this title, and

(ii) to which the FSC is subject.

(4) Disallowance of treaty benefits. -- Any corporation electing to be treated as a FSC under subsection (f)(1) may not claim any benefits under any income tax treaty between the United States and any foreign country.

(5) Coordination with possessions taxation. --

(A) Exemption. -- No tax shall be imposed by any possession of the United States on any foreign trade income derived before January 1, 1987. The preceding sentence shall not apply to any income attributable to the sale of property or the performance of services for ultimate use, consumption, or disposition within the possession.

(B) Clarification that possession may exempt certain income from tax. -- Nothing in any provision of law shall be construed as prohibiting any possession of the United States from exempting from tax any foreign trade income of a FSC or any other income of a FSC described in paragraph (2) or (3) of section 921(d).

(C) No cover over of taxes imposed on FSC. -- Nothing in any provision of law shall be construed as requiring any tax imposed by this title on a FSC to be covered over (or otherwise transferred) to any possession of the United States.

(f) Election of status as FSC (and as small FSC). --

(1) Election. --

(A) Time for making. -- An election by a corporation under section 922(a)(2) to be treated as a FSC, and an election under section 922(b)(1) to be a small FSC, shall be made by such corporation for a taxable year at any time during the 90-day period immediately preceding the beginning of the taxable year, except that the Secretary may give his consent to the making of an election at such other times as he may designate.

(B) Manner of election. -- An election under subparagraph (A) shall be made in such manner as the Secretary shall prescribe and shall be valid only if all persons who are shareholders in such corporation on the first day of the first taxable year for which such election is effective consent to such election.

(2) Effect of election. -- If a corporation makes an election under paragraph (1), then the provisions of this subpart shall apply to such corporation for the taxable year of the corporation for which made and for all succeeding taxable years.

(3) Termination of election. --

(A) Revocation. -- An election under this subsection made by any corporation may be terminated by revocation of such election for any taxable year of the corporation after the first taxable year of the corporation for which the election is effective. A termination under this paragraph shall be effective with respect to such election --

(i) for the taxable year in which made, if made at any time during the first 90 days of such taxable year, or

(ii) for the taxable year following the taxable year in which made, if made after the close of such 90 days, and for all succeeding taxable years of the corporation. Such termination shall be made in such manner as the Secretary shall prescribe by regulations.

(B) Continued failure to be a FSC. -- If a corporation is not a FSC for each of any 5 consecutive taxable years of the corporation for which an election under this subsection is effective, the election to be a FSC shall be terminated and not be in effect for any taxable year of the corporation after such 5th year.

(g) Treatment of shared FSC's. --

(1) In general. -- Except as provided in paragraph (2), each separate account referred to in paragraph (3) maintained by a shared FSC shall be treated as a separate corporation for purposes of this subpart.

(2) Certain requirements applied at shared FSC level. -- Paragraph (1) shall not apply --

(A) for purposes of --

(i) subparagraphs (A), (B), (D), and (E) of section 922(a)(1),

(ii) paragraph (2) of section 922(a),

(iii) subsections (b), (c), and (e) of section 924, and

(iv) subsection (f) of this section, and

(B) for such other purposes as the Secretary may by regulations

prescribe.

(3) Shared FSC. -- For purposes of this subsection, the term "shared FSC" means any corporation if --

(A) such corporation maintains a separate account for transactions with each shareholder (and persons related to such shareholder),

(B) distributions to each shareholder are based on the amounts in the separate account maintained with respect to such shareholder, and

(C) such corporation meets such other requirements as the Secretary may by regulations prescribe.

931. Income from sources within Guam, American Samoa, or the Northern Mariana Islands

(a) General rule. -- In the case of an individual who is a bona fide resident of a specified possession during the entire taxable year, gross income shall not include --

(1) income derived from sources within any specified possession, and

(2) income effectively connected with the conduct of a trade or business by such individual within any specified possession.

(b) Deductions, etc. allocable to excluded amounts not allowable. -- An individual shall not be allowed --

(1) as a deduction from gross income any deductions (other than the deduction under section 151, relating to personal exemptions), or

(2) any credit, properly allocable or chargeable against amounts excluded from gross income under this section.

(c) Specified possession. -- For purposes of this section, the term "specified possession" means Guam, American Samoa, and the Northern Mariana Islands.

(d) Special rules. -- For purposes of this section --
(1) Employees of the United States. -- Amounts paid for services performed as an employee of the United States (or any agency thereof) shall be treated as not described in paragraph (1) or (2) of subsection (a).
(2) Determination of source, etc. -- The determination as to whether income is described in paragraph (1) or (2) of subsection (a) shall be made under regulations prescribed by the Secretary.
(3) Determination of residency. -- For purposes of this section and section 876, the determination of whether an individual is a bona fide resident of Guam, American Samoa, or the Northern Mariana Islands shall be made under regulations prescribed by the Secretary.

932. Coordination of United States and Virgin Islands income taxes
(a) Treatment of United States residents. --
(1) Application of subsection. -- This subsection shall apply to an individual for the taxable year if --
(A) such individual --
(i) is a citizen or resident of the United States (other than a bona fide resident of the Virgin Islands at the close of the taxable year), and
(ii) has income derived from sources within the Virgin Islands, or effectively connected with the conduct of a trade or business within such possession, for the taxable year, or
(B) such individual files a joint return for the taxable year with an individual described in subparagraph (A).
(2) Filing requirement. -- Each individual to whom this subsection applies for the taxable year shall file his income tax return for the taxable year with both the United States and the Virgin Islands.
(3) Extent of income tax liability. -- In the case of an individual to whom this subsection applies in a taxable year for purposes of so much of this title (other than this section and section 7654) as related to the taxes imposed by this chapter, the United States shall be treated as including the Virgin Islands.
(b) Portion of United States tax liability payable to the Virgin Islands.

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(1) In general. -- Each individual to whom subsection (a) applies for the taxable year shall pay the applicable percentage of the taxes imposed by this chapter for such taxable year (determined without regard to paragraph (3)) to the Virgin Islands.

(2) Applicable percentage. --
(A) In general. -- For purposes of paragraph (1), the term "applicable percentage" means the percentage which Virgin Islands adjusted gross income bears to adjusted gross income.

(B) Virgin Islands adjusted gross income. -- For purposes subparagraph (A), the term "Virgin Islands adjusted gross income" means adjusted gross income determined by taking into account only income derived from sources within the Virgin Islands and deductions properly apportioned or allocable thereto.

(3) Amounts paid allowed as credit. -- There shall be allowed as a credit against the tax imposed by this chapter for the taxable year an amount equal to the taxes

required to be paid to the Virgin Islands under paragraph (1) which are so paid.

(c) Treatment of Virgin Islands residents. --

(1) Application of subsection. -- This subsection shall apply to an individual for the taxable year if --

(A) such individual is a bona fide resident of the Virgin Islands at the close of the taxable year, or

(B) such individual files a joint return for the taxable year with an individual described in subparagraph (A).

(2) Filing requirement. -- Each individual to whom this subsection applies for the taxable year shall file an income tax return for the taxable year with the Virgin Islands.

(3) Extent of income tax liability. -- In the case of an individual to whom this subsection applies in a taxable year for purposes of so much of this title 9 (other than this section and section 7654) as relates to the taxes imposed by this chapter, the Virgin Islands shall be treated as including the United States.

(4) Residents of the Virgin Islands. -- In the case of an individual --

(A) who is a bona fide resident of the Virgin Islands at the close of the taxable year,

(B) who, on his return of income tax to the Virgin Islands, reports income from all sources and identifies the source of each item shown on such return, and

(C) who fully pays his tax liability referred to in section 934(a) to the Virgin Islands with respect to such income,

for purposes of calculating income tax liability to the United States, gross income shall not include any amount included in gross income on such return, and allocable deductions and credits shall not be taken into account.

(d) Special rule for joint returns. -- In the case of a joint return, this section shall be applied on the basis of the residence of the spouse who has the greater adjusted gross income (determined without regard to community property laws) for the taxable year.

(e) Special rule for applying section to tax imposed in Virgin Islands.

-- In applying this section for purposes of determining income tax liability incurred to the Virgin Islands, the provisions of this section shall not be affected by the provisions of Federal law referred to in section 934(a).

933.

Income from sources within Puerto Rico

The following items shall not be included in gross income and shall be exempt from taxation under this subtitle:

(1) Resident of Puerto Rico for entire taxable year. -- In the case of an individual who is a bona fide resident of Puerto Rico during the entire taxable year, income derived from sources within Puerto Rico (except amounts received for services performed as an employee of the United States or any agency thereof); but such individual shall not be allowed as a deduction from his gross income any deductions (other than the deduction under section 151, relating to personal exemptions), or any credit, properly allocable to or chargeable against amounts excluded from gross income under this paragraph.

(2) Taxable year of change of residence from Puerto Rico. -- In the case of an individual citizen of the United States who has been a bona fide resident of Puerto Rico for a period of at least 2 years before the date on which he changes his residence from

Puerto Rico, income derived from sources therein (except amounts received for services performed as an employee of the United States or any agency thereof) which is attributable to that part of such period of Puerto Rican residence before such date; but such individual shall not be allowed as a deduction from his gross income any deductions (other than the deduction for personal exemptions under section 151), or any credit, properly allocable to or chargeable against amounts excluded from gross income under this paragraph.