

(iv) Rentals or royalties from property located without the United States or from any interest in such property, including rentals or royalties for the use of, or for the privilege of using, without the United States, patents, copyrights, secret processes and formulas, goodwill, trademarks, trade brands, franchises, and other like property;

(v) Gains, profits, and income from the sale of real property located without the United States; and

(vi) Gains, profits, and income derived from the purchase of personal property within the United States and its sale without the United States.

(2) In applying subparagraph (1)(iv) of this paragraph for taxable years beginning after December 31, 1966, gains described in section 871(a)(1)(D) and section 881(a)(4) from the sale or exchange after October 4, 1966, of patents, copyrights, and other like property shall be treated, as provided in section 871(e)(2), as rentals or royalties for the use of, or privilege of using, property or an interest in property. See paragraph (e) of § 1.871-11.

(3) For determining the time and place of sale of personal property for purposes of subparagraph (1)(vi) of this paragraph, see paragraph (c) of § 1.861-7.

(4) Income derived from the purchase of personal property within the United States and its sale within a possession of the United States shall be treated as derived entirely from within that possession.

(5) If interest is paid on an obligation of a nonresident of the United States by a resident of the United States acting in the resident's capacity as a guarantor of the obligation of the nonresident, the interest will be treated as income from sources without the United States.

(6) For rules treating certain interest as income from sources without the United States, see paragraph (b) of § 1.861-2.

(7) For the treatment of compensation for labor or personal services performed partly within the United States and partly without the United States, see paragraph (b) of § 1.861-4.

(b) *Taxable income.* The taxable income from sources without the United States, in the case of the items of gross

income specified in paragraph (a) of this section, shall be determined on the same basis as that used in § 1.861-8 for determining the taxable income from sources within the United States.

(c) *Income from certain property.* For provisions permitting a taxpayer to elect to treat amounts of gross income attributable to certain aircraft or vessels first leased on or before December 28, 1980, as income from sources within the United States which would otherwise be treated as income from sources without the United States under paragraph (a) of this section, see § 1.861-9. For provisions requiring amounts of gross income attributable to certain aircraft, vessels, or spacecraft first leased by the taxpayer after December 28, 1980, to be treated as income from sources within the United States which would otherwise be treated as income from sources without the United States under paragraph (a) of this section, see § 1.861-9A.

[T.D. 6500, 25 FR 11910, Nov. 26, 1960; 25 FR 14021, Dec. 31, 1960, as amended by T.D. 7378, 40 FR 45434, Oct. 2, 1975; 40 FR 48508, Oct. 16, 1975; T.D. 7928, 48 FR 55847, Dec. 16, 1983]

#### § 1.863-0 Table of contents.

This section lists captions contained in §§ 1.863-1, 1.863-2, and 1.863-3.

##### *§ 1.863-1 Allocation of gross income under section 863(a).*

- (a) In general.
- (b) Natural resources.
  - (1) In general.
  - (2) Additional production prior to export terminal.
  - (3) Definitions.
    - (i) Production activity.
    - (ii) Additional production activities.
    - (iii) Export terminal.
  - (4) Determination of fair market value.
  - (5) Determination of gross income.
  - (6) Tax return disclosure.
  - (7) Examples.
- (c) Determination of taxable income.
- (d) Scholarships, fellowship grants, grants, prizes and awards.
- (e) Residual interest in a REMIC.
  - (1) REMIC inducement fees.
  - (2) Excess inclusion income and net losses.
- (f) *Effective/applicability date.*

##### *§ 1.863-2 Allocation and apportionment of taxable income.*

- (a) Determination of taxable income.
- (b) Determination of source of taxable income.

## § 1.863-1

## 26 CFR Ch. I (4-1-10 Edition)

(c) Effective dates.

### *§ 1.863-3 Allocation and apportionment of income from certain sales of inventory.*

(a) In general.

(1) Scope.

(2) Special rules.

(b) Methods to determine income attributable to production activity and sales activity.

(1) 50/50 method.

(i) Determination of gross income.

(ii) Example.

(2) IFP method.

(i) Establishing an IFP.

(ii) Applying the IFP method.

(iii) Determination of gross income.

(iv) Examples.

(3) Books and records method.

(c) Determination of the source of gross income from production activity and sales activity.

(1) Income attributable to production activity.

(i) Production only within the United States or only within foreign countries.

(A) Source of income.

(B) Definition of production assets.

(C) Location of production assets.

(ii) Production both within the United States and within foreign countries.

(A) Source of income.

(B) Adjusted basis of production assets.

(iii) Anti-abuse rule.

(iv) Examples.

(2) Income attributable to sales activity.

(d) Determination of source of taxable income.

(e) Election and reporting rules.

(1) Elections under paragraph (b) of this section.

(2) Disclosure on tax return.

(f) Income partly from sources within a possession of the United States.

(g) Special rules for partnerships.

(h) Effective dates.

[T.D. 8687, 61 FR 60545, Nov. 29, 1996, as amended by T.D. 9128, 69 FR 26040, May 11, 2004; T. D. 9272, 71 FR 43366, Aug. 1, 2006]

### **§ 1.863-1 Allocation of gross income under section 863(a).**

(a) *In general.* Items of gross income other than those specified in section 861(a) and section 862(a) will generally be separately allocated to sources within or without the United States. See § 1.863-2 for alternate methods to determine the income from sources within or without the United States in the case of items specified in § 1.863-2(a). See also sections 865(b) and (e)(2). In the case of sales of property involv-

ing partners and partnerships, the rules of § 1.863-3(g) apply.

(b) *Natural resources—(1) In general.* Notwithstanding any other provision, except to the extent provided in paragraph (b)(2) of this section, gross receipts from the sale outside the United States of products derived from the ownership or operation of any farm, mine, oil or gas well, other natural deposit, or timber within the United States, must be allocated between sources within and without the United States based on the fair market value of the product at the export terminal (as defined in paragraph (b)(3)(iii) of this section). Notwithstanding any other provision, except to the extent provided in paragraph (b)(2) of this section, gross receipts from the sale within the United States of products derived from the ownership or operation of any farm, mine, oil or gas well, other natural deposit, or timber outside the United States must be allocated between sources within and without the United States based on the fair market value of the product at the export terminal. For place of sale, see §§ 1.861-7(c) and 1.863-3(c)(2). The source of gross receipts equal to the fair market value of the product at the export terminal will be from sources where the farm, mine, well, deposit, or uncut timber is located. The source of gross receipts from the sale of the product in excess of its fair market value at the export terminal (excess gross receipts) will be determined as follows—

(i) If the taxpayer engages in additional production activities subsequent to shipment from the export terminal and outside the country of sale, the source of excess gross receipts must be determined under § 1.863-3. For purposes of applying § 1.863-3, only production assets used in additional production activity subsequent to the export terminal are taken into account.

(ii) In all other cases, excess gross receipts will be from sources within the country of sale. This paragraph (b)(1)(ii) applies to a taxpayer that engages in additional production activities in the country of sale, as well as to a taxpayer that does not engage in additional production activities at all.

(2) *Additional production prior to export terminal.* Notwithstanding any