

- (B) Inadvertent error.
- (iv) Liabilities of insurance companies.
- (v) Liabilities used to increase artificially interest expense on U.S. booked liabilities.
- (vi) Hedging transactions.
- (vii) Amount of U.S. booked liabilities of a partner.
- (viii) Interbranch transactions.
- (3) Average total amount of U.S. booked liabilities.
- (4) Interest expense where U.S. booked liabilities equal or exceed U.S. liabilities.
 - (i) In general.
 - (ii) Scaling ratio.
 - (iii) Special rules for insurance companies.
- (5) U.S.-connected interest rate where U.S. booked liabilities are less than U.S.-connected liabilities.
 - (i) In general.
 - (ii) Interest rate on excess U.S.-connected liabilities.
 - (A) General rule.
 - (B) Annual published rate election.
 - (6) Examples.
 - (e) Separate currency pools method.
 - (1) General rule.
 - (i) Determine the value of U.S. assets in each currency pool.
 - (ii) Determine the U.S.-connected liabilities in each currency pool.
 - (iii) Determine the interest expense attributable to each currency pool.
 - (2) Prescribed interest rate.
 - (3) Hedging transactions.
 - (4) Election not available if excessive hyperinflationary assets.
 - (5) Examples.
 - (f) Effective date.
 - (1) General rule.
 - (2) Special rules for financial products.

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§ 1.882-1 Taxation of foreign corporations engaged in U.S. business or of foreign corporations treated as having effectively connected income.

(a) *Segregation of income.* This section applies for purposes of determining the tax of a foreign corporation which 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 foreign corporation which at no time during the taxable year is engaged in trade or business in the United States but has for the taxable year real property income or interest on obligations of the United States which, by reason of section 882 (d) or (e) and § 1.882-2, is

treated as effectively connected for the taxable year with the conduct of a trade or business in the United States by that corporation. A foreign corporation to which this section applies must segregate its gross income for the taxable year into two categories, namely, the income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by that corporation and 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 corporation. 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 foreign corporation 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 882 (d) or (e) and § 1.882-2 as income which is effectively connected for the taxable year with the conduct of a trade or business in the United States by the foreign corporation.

(b) *Imposition of tax—(1) Income not effectively connected with the conduct of a trade or business in the United States.* If a foreign corporation to which this section applies derives during the taxable year from sources within the United States income or gains described in section 881(a) and paragraph (b) or (c) of § 1.881-2 which are not effectively connected for the taxable year with the conduct of a trade or business in the United States by that corporation, 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 § 1.881-2 as though the income or gains were derived by a foreign corporation not engaged in trade or business in the United States during the taxable year, except that in applying paragraph (c) of such section there

shall not be taken into account any gains which are taken into account in determining the tax under section 882(a)(1) and subparagraph (2) of this paragraph.

(2) *Income effectively connected with the conduct of a trade or business in the United States*—(i) *In general.* If a foreign corporation to which 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 corporation, the taxable income or gains shall, except as provided in § 1.871-12, be taxed in accordance with section 11 or, in the alternative, section 1201(a). See sections 11(f) and 882(a)(1). Any income of the foreign corporation which is not effectively connected for the taxable year with the conduct of a trade or business in the United States by that corporation shall not be taken into account in determining either the rate or amount of such tax.

(ii) *Determination of taxable income.* The taxable income for any taxable year for purposes of this subparagraph consists only of the foreign corporation'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 corporation; 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 corporation 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 corporation.

(iii) *Cross references.* For rules for determining the gross income and deductions for the taxable year, see section 882 (b) and (c)(1) and the regulations thereunder.

(c) *Change in trade or business status.* The principles of paragraph (c) of § 1.871-8 shall apply to cases where

there has been a change in the trade or business status of a foreign corporation.

(d) *Credits against tax.* The credits allowed by section 32 (relating to tax withheld at source on foreign corporations), section 33 (relating to the foreign tax credit), 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 6042 (relating to overpayments of a 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 881(a) and paragraph (b)(1) 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 882(c)(2) and the regulations thereunder.

(e) *Payment of estimated tax.* Every foreign corporation which for the taxable year is subject to tax under section 11 or 1201(a) and this section must make payment of its estimated tax in accordance with section 6154 and the regulations thereunder. In determining the amount of the estimated tax the foreign corporation must treat the tax imposed by section 881(a) and paragraph (b)(1) of this section as though it were a tax imposed by section 11.

(f) *Effective date.* This section applies for taxable years beginning after December 31, 1966. For corresponding rules applicable to taxable years beginning before January 1, 1967, see 26 CFR 1.882-1 (Revised as of January 1, 1971).

[T.D. 7293, 38 FR 32797, Nov. 28, 1973]

§ 1.882-2 Income of foreign corporations treated as effectively connected with U.S. business.

(a) *Election as to real property income.* A foreign corporation which during the taxable year derives any income from real property which is located in the United States, or derives income from any interest in any such real property, may elect, pursuant to section 882(d) and § 1.871-10, to treat all such income