

(h) through (k) [Reserved] For further guidance, see § 1.860G-2(h) through (k).

[T.D. 9533, 76 FR 39282. July 6, 2011]

**§ 1.860G-3 Treatment of foreign persons.**

(a) *Transfer of a residual interest with tax avoidance potential*—(1) *In general.* A transfer of a residual interest that has tax avoidance potential is disregarded for all Federal tax purposes if the transferee is a foreign person. Thus, if a residual interest with tax avoidance potential is transferred to a foreign holder at formation of the REMIC, the sponsor is liable for the tax on any excess inclusion that accrues with respect to that residual interest.

(2) *Tax avoidance potential*—(i) *Defined.* A residual interest has tax avoidance potential for purposes of this section unless, at the time of the transfer, the transferor reasonably expects that, for each excess inclusion, the REMIC will distribute to the transferee residual interest holder an amount that will equal at least 30 percent of the excess inclusion, and that each such amount will be distributed at or after the time at which the excess inclusion accrues and not later than the close of the calendar year following the calendar year of accrual.

(ii) *Safe harbor.* For purposes of paragraph (a)(2)(i) of this section, a transferor has a reasonable expectation if the 30-percent test would be satisfied were the REMIC's qualified mortgages to prepay at each rate within a range of rates from 50 percent to 200 percent of the rate assumed under section 1272(a)(6) with respect to the qualified mortgages (or the rate that would have been assumed had the mortgages been issued with original issue discount).

(3) *Effectively connected income.* Paragraph (a)(1) of this section will not apply if the transferee's income from the residual interest is subject to tax under section 871(b) or section 882.

(4) *Transfer by a foreign holder.* If a foreign person transfers a residual interest to a United States person or a foreign holder in whose hands the income from a residual interest would be effectively connected income, and if the transfer has the effect of allowing the transferor to avoid tax on accrued

excess inclusions, then the transfer is disregarded and the transferor continues to be treated as the owner of the residual interest for purposes of section 871(a), 881, 1441, or 1442.

(b) *Accounting for REMIC net income*—(1) *Allocation of partnership income to a foreign partner.* A domestic partnership shall separately state its allocable share of REMIC taxable income or net loss in accordance with § 1.702-1(a)(8). If a domestic partnership allocates all or some portion of its allocable share of REMIC taxable income to a partner that is a foreign person, the amount allocated to the foreign partner shall be taken into account by the foreign partner for purposes of sections 871(a), 881, 1441, and 1442 as if that amount was received on the last day of the partnership's taxable year, except to the extent that some or all of the amount is required to be taken into account by the foreign partner at an earlier time under section 860G(b) as a result of a distribution by the partnership to the foreign partner or a disposition of the foreign partner's indirect interest in the REMIC residual interest. A disposition in whole or in part of the foreign partner's indirect interest in the REMIC residual interest may occur as a result of a termination of the REMIC, a disposition of the partnership's residual interest in the REMIC, a disposition of the foreign partner's interest in the partnership, or any other reduction in the foreign partner's allocable share of the portion of the REMIC net income or deduction allocated to the partnership. See § 1.871-14(d)(2) for the treatment of interest received on a regular or residual interest in a REMIC. For a partnership's withholding obligations with respect to excess inclusion amounts described in this paragraph (b)(1), see §§ 1.1441-2(b)(5), 1.1441-2(d)(4), 1.1441-5(b)(2)(i)(A), and §§ 1.1446-1 through 1.1446-7.

(2) *Excess inclusion income allocated by certain pass-through entities to a foreign person.* If an amount is allocated under section 860E(d)(1) to a foreign person that is a shareholder of a real estate investment trust or a regulated investment company, a participant in a common trust fund, or a patron of an organization to which part I of subchapter

T applies and if the amount so allocated is governed by section 860E(d)(2) (treating it “as an excess inclusion with respect to a residual interest held by” the taxpayer), the amount shall be taken into account for purposes of sections 871(a), 881, 1441, and 1442 at the same time as the time prescribed for other income of the shareholder, participant, or patron from the trust, company, fund, or organization.

[T.D. 8458, 57 FR 61313, Dec. 24, 1992, as amended by T.D. 9272, 71 FR 43365, Aug. 1, 2006; T.D. 9415, 73 FR 40172, July 14, 2008]

TAX BASED ON INCOME FROM  
SOURCES WITHIN OR WITHOUT  
THE UNITED STATES

DETERMINATION OF SOURCES OF INCOME

**§ 1.861-1 Income from sources within  
the United States.**

(a) *Categories of income.* Part I (section 861 and following), subchapter N, chapter 1 of the Code, and the regulations thereunder determine the sources of income for purposes of the income tax. These sections explicitly allocate certain important sources of income to the United States or to areas outside the United States, as the case may be; and, with respect to the remaining income (particularly that derived partly from sources within and partly from sources without the United States), authorize the Secretary or his delegate to determine the income derived from sources within the United States, either by rules of separate allocation or by processes or formulas of general apportionment. The statute provides for the following three categories of income:

(1) *Within the United States.* The gross income from sources within the United States, consisting of the items of gross income specified in section 861(a) plus the items of gross income allocated or apportioned to such sources in accordance with section 863(a). See §§ 1.861-2 to 1.861-7, inclusive, and § 1.863-1. The taxable income from sources within the United States, in the case of such income, shall be determined by deducting therefrom, in accordance with sections 861(b) and 863(a), the expenses, losses, and other deductions properly apportioned or allocated thereto and a rat-

able part of any other expenses, losses, or deductions which cannot definitely be allocated to some item or class of gross income. See §§ 1.861-8 and 1.863-1.

(2) *Without the United States.* The gross income from sources without the United States, consisting of the items of gross income specified in section 862(a) plus the items of gross income allocated or apportioned to such sources in accordance with section 863(a). See §§ 1.862-1 and 1.863-1. The taxable income from sources without the United States, in the case of such income, shall be determined by deducting therefrom, in accordance with sections 862(b) and 863(a), the expenses, losses, and other deductions properly apportioned or allocated thereto and a ratable part of any other expenses, losses, or deductions which cannot definitely be allocated to some item or class of gross income. See §§ 1.862-1 and 1.863-1.

(3) *Partly within and partly without the United States.* The gross income derived from sources partly within and partly without the United States, consisting of the items specified in section 863(b) (1), (2), and (3). The taxable income allocated or apportioned to sources within the United States, in the case of such income, shall be determined in accordance with section 863 (a) or (b). See §§ 1.863-2 to 1.863-5, inclusive.

(4) *Exceptions.* An owner of certain aircraft or vessels first leased on or before December 28, 1980, may elect to treat income in respect of these aircraft or vessels as income from sources within the United States for purposes of sections 861(a) and 862(a). See § 1.861-9. An owner of certain aircraft, vessels, or spacecraft first leased after December 28, 1980, must treat income in respect of these craft as income from sources within the United States for purposes of sections 861(a) and 862(a). See § 1.861-9A.

(b) *Taxable income from sources within the United States.* The taxable income from sources within the United States shall consist of the taxable income described in paragraph (a)(1) of this section plus the taxable income allocated or apportioned to such sources, as indicated in paragraph (a)(3) of this section.