amounts so received being credited to its surplus account or to a special capital account, such amounts will not be considered income, although there is no increase in the outstanding shares of stock of the corporation. The payments under such circumstances are in the nature of voluntary assessments upon, and represent an additional price paid for, the shares of stock held by the individual shareholders, and will be treated as an addition to and as a part of the operating capital of the company. (See articles 22 (a)–14 and 24–2.)

ART. 22 (a)–18. *Sale and purchase by corporation of its bonds.*—(1) (*a*) If bonds are issued by a corporation at their face value, the corporation realizes no gain or loss. (*b*) If the corporation purchases any of such bonds at a price in excess of the issuing price or face value, the excess of the purchase price over the issuing price or face value is a deductible expense for the taxable year. (*c*) If, however, the corporation purchases any of such bonds at a price less than the issuing price or face value, the excess of the issuing price or face value over the purchase price is gain or income for the taxable year.

(2) (*a*) If, subsequent to February 28, 1913, bonds are issued by a corporation at a premium, the net amount of such premium is gain or income which should be prorated or amortized over the life of the bonds. (*b*) If the corporation purchases any of such bonds at a price in excess of the issuing price minus any amount of premium already returned as income, the excess of the purchase price over the issuing price minus any amount of premium already returned as income (or over the face value plus any amount of premium not yet returned as income) is a deductible expense for the taxable year. (*c*) If, however, the corporation purchases any of such bonds at a price less than the issuing price minus any amount of premium already returned as income, the excess of the issuing price, minus any amount of premium already returned as income (or of the face value plus any amount of premium not yet returned as income), over the purchase price is gain or income for the taxable year.

(3) (*a*) If bonds are issued by a corporation at a discount, the net amount of such discount is deductible and should be prorated or amortized over the life of the bonds. (*b*) If the corporation purchases any of such bonds at a price in excess of the issuing price plus any amount of discount already deducted, the excess of the purchase price over the issuing price plus any amount of discount already deducted (or over the face value minus any amount of discount not yet deducted) is a deductible expense for the taxable year. (*c*) If, however, the corporation purchases any of such bonds at a price less than the issuing price plus any amount of discount already deducted, the excess of the issuing price, plus any amount of discount already deducted (or of the face value minus any amount of discount not yet deducted), over the purchase price is gain or income for the taxable year.

(4) (*a*) If bonds were issued by a corporation prior to March 1, 1913, at a premium, the net amount of such premium was gain or income for the year in which the bonds were issued and should not be prorated or amortized over the life of the bonds. (*b*) If the corporation purchases any of such bonds at a price in excess of the face value of the bonds, the excess of the purchase price over the face value is a deductible expense for the taxable year. (*c*) If, however, the corporation purchases any of such bonds at a price less than the face value the excess of the face value over the purchase price is gain or income for the taxable year.

ART. 22 (a)–19. *Sale of capital assets by corporation.*—If property is acquired and later sold for an amount in excess of the cost or other basis, the gain on the sale is income. If, then, a corporation sells its capital assets in whole or in part, it shall include in its gross income for the year in which the sale was made the gain from such sale, computed as provided in sections 111–113. If the purchaser takes over all the assets and assumes the liabilities, the amount so assumed is part of the selling price.

ART. 22 (a)–20. *Income to lessor corporation from leased property.*—If a corporation has leased its property in consideration that the lessee shall pay in lieu of other rental an amount equivalent to a certain rate of dividend on the lessor's capital stock or the interest on the lessor's outstanding indebtedness, together with taxes, insurance, or other fixed charges, such payments shall be considered rental payments and shall be returned by the lessor corporation as income, notwithstanding the fact that the dividends and interest are paid by the lessee directly to the shareholders and bondholders of the lessor. The fact that a corporation has conveyed or let its property and has parted with its management and control, or has ceased to engage in the business for which it was originally organized, will not relieve it from liability to the tax. While the payments made by the lessee directly to the bondholders or shareholders of the lessor are rentals as to both the lessee and lessor (rentals paid in one case and rentals received in the other), to the bondholders and the shareholders such amounts are interest and dividend payments received as from the lessor and as such shall be accounted for in their returns.

ART. 22 (a)–21. *Gross income of corporation in liquidation.*—When a corporation is dissolved, its affairs are usually wound up by a receiver or trustees in dissolution. The corporate existence is continued for the purpose of liquidating the assets and paying the debts, and such receiver or trustees stand in the stead of the corporation for such purposes. (See sections 274 and 298.) Any sales of property by them are to be treated as if made by the corporation for the purpose of ascertaining the gain or loss. No gain or loss is realized by a corporation from the mere distribution of its assets in kind in partial or complete liquidation, however they may have appreciated or depreciated in value since their acquisition. But see section 44 (d) and article 44–5. (See further article 52–2.)

[SEC. 22. *Gross income.*]

(*b*) *Exclusions from gross income.*—The following items shall not be included in gross income and shall be exempt from taxation under this title:

ART. 22 (b)–1. *Exemptions—Exclusions from gross income.*—Certain items of income specified in section 22 (b) are exempt from tax and may be excluded from gross income. These items, however, are exempt only to the extent and in the amount specified. No other items are exempt from gross income except (1) those items of income which are, under the Constitution, not taxable by the Federal Government; (2) those items of income which are exempt from tax on income under the provisions of any Act of Congress not inconsistent with or repealed by the Act; (3) the income exempted under the provisions of section 116. Since the tax is imposed on net income, the exemption referred to above is not to be confused with the deductions allowed by section 23 and other provisions of the Act to be made from gross income in computing net income. As to other items not to be included in gross income, see sections 112 and 119 and Supplements G, H. I, and J.

[SEC. 22. *Gross income.*]

[(*b*) *Exclusions from gross income.*—The following items shall not be included in gross income and shall be exempt from taxation under this title:]

(1) *Life insurance.*—Amounts received under a life insurance contract paid by reason of the death of the insured, whether in a single sum or otherwise (but if such amounts are held by the insurer under an agreement to pay interest thereon, the interest payments shall be included in gross income);

ART. 22 (b) (1)–1. *Life insurance—Amounts paid by reason of the death of the insured.*—The proceeds of life insurance policies, paid by reason of the death of an insured to his estate or to any beneficiary (individual, partnership, or corporation, but not a transferee for valuable consideration), directly or in trust, are excluded from the gross income of the beneficiary. While it is immaterial whether the proceeds of a life insurance policy payable upon the death of the insured are paid to the beneficiary in a single sum or in installments, only the amount paid solely by reason of the death of the insured is exempted. The amount exempted is the amount payable had the insured or the beneficiary not elected to exercise an option to receive the proceeds of the policy or any part thereof at a latter date or dates. If the policy provides no option for payment

and $4,500, respectively, were paid out of the earnings and profits accumulated after February 28, 1913, and prior to the taxable year, as follows:

Distributions during 1938		Portion out of earnings or profits of the taxable year	Portion out of earnings accumulated since Feb. 28, 1913, and prior to taxable year	Taxable amount of each distribution
Date	Amount			
Mar. 10	$15,000	$7,500	$7,500	$15,000
June 10	15,000	7,500	4,500	12,000
Sept. 10	15,000	7,500	----------	7,500
Dec. 10	15,000	7,500	----------	7,500
Total amount taxable as dividends				42,000

Any distribution by a corporation out of earnings or profits accumulated prior to March 1, 1913, or out of increase in value of property accrued prior to March 1, 1913 (whether or not realized by sale or other disposition, and, if realized, whether prior to or on or after March 1, 1913), is not a dividend within the meaning of Title I.

ART. 115–3. *Earnings or profits.*—In determining the amount of earnings or profits (whether of the taxable year, or accumulated since February 28, 1913, or accumulated prior to March 1, 1913) due consideration must be given to the facts, and mere bookkeeping entries increasing or decreasing surplus will not be conclusive. Among the items entering into the computation of corporate earnings or profits for a particular period are all income exempted by statute, income not taxable by the Federal Government under the Constitution, as well as all items includible in gross income under section 22 (a) of the Act or corresponding provisions of prior Acts. Gains and losses within the purview of section 112 or corresponding provisions of prior Acts are brought into the earnings and profits at the time and to the extent such gains and losses are recognized under that section. Interest on State bonds and certain other obligations, although not taxable when received by a corporation, is taxable to the same extent as other dividends when distributed to shareholders in the form of dividends.

In the case of a corporation in which depletion is a factor in the determination of income, the only depletion deductions to be considered in the computation of earnings or profits are those based on (1) cost or other basis, if the depletable asset was acquired subsequent to February 28, 1913, or (2) adjusted cost or March 1, 1913, value, whichever is higher, if acquired prior to March 1, 1913. Thus, discovery and percentage depletion under all Revenue Acts for mines and oil and gas wells should not be taken into consideration in computing the earnings or profits of a corporation.

A loss sustained for a year prior to the taxable year does not affect the earnings or profits of the taxable year. However, in determining the earnings or profits accumulated since February 28, 1913, the excess of a loss sustained for a year subsequent to February 28, 1913, over the undistributed earnings or profits accumulated since February 28, 1913, and prior to the year for which the loss was sustained, reduces surplus as of March 1, 1913, to the extent of such excess. And, if the surplus as of March 1, 1913, was sufficient to absorb such excess, distributions to shareholders after the year of the loss are out of earnings or profits accumulated since the year of the loss to the extent of such earnings.

With respect to the effect on the earnings or profits accumulated since February 28, 1913, of distributions made on or after January 1, 1916, and prior to August 6, 1917, out of earnings or profits accumulated prior to March 1, 1913, which distributions were specifically declared to be out of earnings or profits accumulated prior to March 1, 1913, see section 31 (b) of the Revenue Act of 1916, as amended by section 1211 of the Revenue Act of 1917.

ART. 115–4. *Distributions other than a dividend.*—Under section 115 (d), any distribution (including a distribution out of earnings or profits accumulated before March 1, 1913) other than

(1) a dividend (see articles 115–1 and 115–2),

(2) a distribution out of increase in value of property accrued prior to March 1, 1913 (see article III–1), or

(3) a distribution in partial or complete liquidation (see article 115–5)

shall be applied against and reduce the adjusted basis of the stock provided in section 113 and shall be taxable to the recipient if, and to the extent that, such distribution exceeds such basis. The provisions of this article are applicable to such distributions received by one corporation from another corporation.

Example: In 1938 the M Corporation purchased certain shares of stock in the O Corporation for $10,000. During that year the M Corporation received a distribution from the O Corporation of $2,000 paid out of earnings or profits of the O Corporation accumulated prior to March 1, 1913. This distribution must be applied by the M Corporation against the basis of its stock in the O Corporation reducing such basis to $8,000. The $2,000 does not constitute a part of the earnings or profits of the M Corporation. If the M Corporation subsequently sells the stock of the O Corporation for $9,000, it realizes a gain of $1,000, which constitutes a part of its earnings or profits for the year in which the stock is sold. If the distribution had amounted to $14,000, the gain of $4,000 would be taxable to the M Corporation and would have constituted a part of the earnings or profits of that corporation for the year in which the distribution was made.

ART. 115–5. *Distributions in liquidation.*—(a) *General.*—Amounts distributed in complete liquidation of a corporation are to be treated as in full payment in exchange for the stock, and amounts distributed in partial liquidation are to be treated as in part or full payment in exchange for the stock so canceled or redeemed. The gain or loss to a shareholder from a distribution in liquidation is to be determined, as provided in section 111 and article 111–1, by comparing the amount of the distribution with the cost or other basis of the stock provided in section 113; but the gain or loss will be recognized only to the extent provided in section 112.

(b) *Complete liquidation.*—In the case of amounts distributed in complete liquidation of a corporation, the amount of the gain or loss so recognized is subject in general to the limitations contained in section 117. For this purpose the term "complete liquidation" includes any one of a series of distributions made by a corporation in complete cancellation or redemption of all of its stock in accordance with a bona fide plan of liquidation and under which the transfer of the property under the liquidation is to be completed within a time specified in the plan, not exceeding, from the close of the taxable year during which is made the first of the series of distributions under the plan, (1) three years if the first of such series of distributions is made in a taxable year beginning after December 31, 1937, or (2) two years, if the first of such series of distributions was made in a taxable year beginning prior to January 1, 1938.

For the purposes of the last sentence of section 115 (c), a liquidation may be completed prior to the actual dissolution of the liquidating corporation but no liquidation is completed until the liquidating corporation and the receiver or trustees in liquidation are finally divested of all the property (both tangible and intangible).

For the purpose of this article the determination of whether a foreign corporation was a foreign personal holding company with respect to a taxable year beginning on or before, and ending after August 26, 1937, shall be made under section 331 of the Revenue Act of 1936, added to such Act by section 201 of the Revenue Act of 1937, and articles 331–1, 331–2, and 331–3 of Chapter XXXIV, added to Regulations 94 by Treasury Decision 4782, approved December 7, 1937 (C. B. 1937–2, p. 163).

Example: A, an individual whose taxable year is the calendar year, owns 20 shares of stock of the N Corporation, a domestic corporation, 10 shares of which were acquired in 1924 at a cost of $1,250 and the balance of 10 shares in June.

governments (other than ambassadors, ministers and members of their households including secretaries, attachés and servants) from sources other than their salaries, fees, or wages, referred to above, is subject to Federal income tax. The compensation of citizens of the United States who are officers or employees of a foreign government is not exempt from income tax. (But see section 116 (a).) Under the provisions of the tax convention between the United States and France, and without regard to any other provision of this article, compensation paid by France to French citizens for labor or personal services performed in the United States is exempt from Federal income tax. (See page 680 of the Appendix to these regulations.)

ART. 116-2. *Compensation of State officers and employees.*—Compensation received for services rendered to a State is to be included in gross income unless the person receives such compensation from the State as an officer or employee thereof and such compensation is immune from taxation under the Constitution of the United States.

One is not an officer or employee of a State merely by reason of rendering services to the State and receiving compensation therefor. Persons employed by a State, under a contract for the rendering of services of a special nature, such as those performed by a consulting engineer who is employed to advise a State with respect to water supply or sewage disposal systems, whose duties are prescribed by the contract and whose work is not of a permanent or continuous character, are not officers or employees of the State.

If all or part of the compensation of an officer or employee of a State is paid directly or indirectly by the United States, such compensation (or part) is taxable, as, for example, any compensation paid by the United States to officers of the National Guard of a State, or compensation paid by a State to officers or employees of an agricultural school or college wholly or partly out of grants from the United States.

The commissions of receivers appointed by the State courts and the fees received by notaries public are taxable. As used in this article, the term "State" includes a political subdivision of a State.

ART. 116-3. *Bridges to be acquired by State or political subdivisions.*—(1) Any State or political subdivision thereof claiming a refund under the provisions of section 116 (e) of an amount equal to all or a portion of any income tax levied, assessed, collected, and paid in the manner and at the rates prescribed in Title I, shall file a claim therefor on Form 843 (to which there shall be attached as exhibits the matter hereinafter prescribed) with the collector of internal revenue for the district in which the tax was paid, which claim shall be executed on behalf of such State or political subdivision thereof by the treasurer or other fiscal officer thereof and shall contain—

(*a*) A statement of the name of the taxpayer, of the amount of tax levied, assessed, collected, and paid for the taxable year or period in respect of which the claim is made, and the amount of refund thereby sought;

(*b*) A full statement of the facts considered by the claimant sufficient to entitle it to receive the refund, including copies of all contracts and other documents bearing on the case, and a statement that the claim is submitted under the provisions of section 116 (e);

(*c*) A showing which will establish to the satisfaction of the Commissioner that the fiscal officer presenting the claim has authority to receive the amount of the refund on behalf of the State or political subdivision which he assumes to represent and to apply without delay the entire amount of such refund in part payment for the acquisition of such bridge, including copies of the laws, ordinances, or similar enactments considered by the claimant sufficient to establish its authority to receive the refund and so to apply it, together with a statement that such fiscal officer will receive and immediately so apply the entire amount of the refund; and

(*d*) An affidavit made by or on behalf of the taxpayer, which affidavit shall state that the taxpayer thereby joins with and concurs in the request of the State or political subdivision thereof that a refund of an amount equal to all or a portion of the tax previously paid by such taxpayer be made to such State or political subdivision, that the taxpayer agrees to receive the amount refunded from the State or political subdivision to which it is paid and immediately to apply the entire amount of such refund in part payment for the acquisition of such bridge, and that if for any reason the contract which is the basis of the claim for refund is not fully executed and performed, the taxpayer will repay to the United States upon its demand the entire amount of the refund with interest at 6 percent per annum from the date the refund is made without seeking or claiming the benefit of any statute of limitations which prior thereto may have run against the United States.

(2) No refund shall be made of any amount in excess of the amount of the tax levied, assessed, collected, and paid by the taxpayer for any taxable year or period. A separate claim shall be made in respect of each separate taxable year or period. If by the terms of the contract on which the claim is based two or more States or political subdivisions of a State or States are entitled to acquire the bridge, the claim for refund in respect of each separate taxable year or period must be made jointly by the States or political subdivisions thereof so entitled. The amount refunded under section 116 (e) and this article is not considered an overpayment within the meaning of section 614 of the Revenue Act of 1928 (paragraph 42 of the Appendix to these regulations), relating to interest on overpayments, and no interest shall be allowed or paid upon the amount of the refund.

(3) A check or voucher in payment of a claim for refund allowed under section 116 (e) will be drawn in the name of the fiscal officer or officers having authority, as established under paragraph (1) (*c*) hereof, to receive the same, and will contain an express provision that it is issued for the sole purpose and subject to the conditions prescribed in that section and this article.

CHAPTER XVII

Capital Gains and Losses

SEC. 117. *Capital gains and losses.*—(a) *Definitions.*—As used in this title—

(1) *Capital assets.*—The term "capital assets" means property held by the taxpayer (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business, of a character which is subject to the allowance for depreciation provided in section 23 (l);

(2) *Short-term capital gain.*—The term "short-term capital gain" means gain from the sale or exchange of a capital asset held for not more than 18 months, if and to the extent such gain is taken into account in computing net income;

(3) *Short-term capital loss.*—The term "short-term capital loss" means loss from the sale or exchange of a capital asset held for not more than 18 months, if and to the extent such loss is taken into account in computing net income;

(4) *Long-term capital gain.*—The term "long-term capital gain" means gain from the sale or exchange of a capital asset held for more than 18 months, if and to the extent such gain is taken into account in computing net income;

(5) *Long-term capital loss.*—The term "long-term capital loss" means loss from the sale or exchange of a capital asset held for more than 18 months, if and to the extent such loss is taken into account in computing net income;

(6) *Net short-term capital gain.*—The term "net short-term capital gain" means the excess of short-term capital gains for the taxable year over the sum of (A) short-term capital losses for the taxable year, plus (B) the net short-term capital loss of the preceding taxable year, to the extent brought forward to the taxable year under subsection (c);

(7) *Net short-term capital loss.*—The term "net short-term capital loss" means the excess of short-term capital losses for the taxable year over the short-term capital gains for such year;

(8) *Net long-term capital gain.*—The term "net long-term capital gain" means the excess of long-term capital gains for the taxable year over the long-term capital losses for such year;

(9) *Net long-term capital loss.*—The term "net long-term capital loss" means the excess of long-term capital losses for the taxable year over the long-term capital gains for such year.

(b) *Percentage taken into account.*—In the case of a taxpayer, other than a corporation, only the following percentages of the gain or loss recognized upon the sale or ex-

Whether a nonresident alien has an "office or place of business" within the United States depends upon the facts in a particular case. The term "office or place of business," however, implies a place for the regular transaction of business and does not include a place where casual or incidental transactions might be, or are, effected.

Neither the beneficiary nor the grantor of a trust, whether revocable or irrevocable, is deemed to be engaged in trade or business in the United States or to have an office or place of business therein, merely because the trustee is engaged in trade or business in the United States or has an office or place of business therein.

SEC. 212. *Gross income.*—(a) *General rule.*—In the case of a nonresident alien individual gross income includes only the gross income from sources within the United States.

(b) *Ships under foreign flag.*—The income of a nonresident alien individual which consists exclusively of earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States and to corporations organized in the United States shall not be included in gross income and shall be exempt from taxation under this title.

ART. 212–1. *Gross income of nonresident individuals.*—In general, in the case of nonresident alien individuals "gross income" means only the gross income from sources within the United States, determined under the provisions of section 119. (See articles 119–1 to 119–14.) The items of gross income from sources without the United States and therefore not taxable to nonresident aliens are described in section 119 (c). As to who are nonresident alien individuals see articles 211–2 to 211–6.

Income received by a resident alien from sources without the United States is taxable although such person may become a nonresident alien subsequent to its receipt and prior to the close of the taxable year. Conversely, income received by a nonresident alien from sources without the United States is not taxable though such person may become a resident alien subsequent to its receipt and prior to the close of the taxable year.

(a) No United States business or office.—The gross income of a nonresident alien individual not engaged in trade or business within the United States and not having an office or place of business therein at any time during the taxable year, whether such alien comes within section 211 (a) or section 211 (c), is gross income from sources within the United States consisting of fixed or determinable annual or periodical income. His taxable income does not include profits derived from the effecting of transactions in the United States in stocks, securities or commodities (including hedging transactions) through a resident broker, commission agent, or custodian, or profits derived from the sale within the United States of personal property or real property located therein.

(b) United States business or office.—The gross income of a nonresident alien individual who at any time within the taxable year was engaged in trade or business within the United States or had an office or place of business therein is not limited to the items of gross income specified in section 211 (a), but includes any item of gross income which is treated as income from sources within the United States, except those items which are exempt from taxation by statute or treaty or which are not taxable by the Federal Government under the Constitution. (See sections 22 (b), 112, 116, 119, and 212 (b).)

In general, any nonresident alien individual who performs personal services within the United States is considered as being engaged in trade or business within the United States and therefore his net income from sources within the United States, including his compensation, is subject to the normal tax of 4 percent and the surtax. However, the phrase "engaged in trade or business within the United States" does not apply to the personal services performed within the United States for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate $3,000. Such compensation is not income from sources within the United States. (See section 119 (a) (3).) As to the exclusion from gross income of the official compensation received by employees of foreign governments see section 116 (h).

The effecting of transactions in the United States in stocks, securities, or commodities (including hedging transactions) through a resident broker, commission agent, or custodian does not bring a nonresident alien individual within the class of nonresident alien individuals engaged in trade or business within the United States, but if a nonresident alien individual by reason of rendering personal services in the United States, or for other reasons, is classed as a nonresident alien individual engaged in trade or business within the United States or having an office or place of business therein, he is taxable upon all income from sources within the United States, including profits derived from the effecting of such transactions. Such a nonresident alien individual is required to include in gross income capital gains, gains from hedging transactions, and profits derived from the sale within the United States of personal property, or of real property located therein.

ART. 212–2. *Exclusion of earnings of foreign ships from gross income.*—So much of the income from sources within the United States of a nonresident alien individual who at any time within the taxable year was engaged in trade or business within the United States, or had an office or place of business therein as consists of earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States nonresident in such foreign country and to corporations organized in the United States, shall not be included in gross income. Foreign countries which either impose no income tax, or, in imposing such tax, exempt from taxation so much of the income of a citizen of the United States nonresident in such foreign country and of a corporation organized in the United States as consists of earnings derived from the operation of a ship or ships documented under the laws of the United States are considered as granting an equivalent exemption within the meaning of this article.

A nonresident alien individual not engaged in trade or business within the United States and not having an office or place of business therein at any time within the taxable year is not required to include in gross income such income from sources within the United States as is derived from the operation of a ship or ships, whether or not the foreign country under the laws of which such ships are documented meets the equivalent exemption requirements of the statute.

SEC. 213. *Deductions.*—(a) *General rule.*—In the case of a nonresident alien individual the deductions shall be allowed only if and to the extent that they are connected with income from sources within the United States; and the proper apportionment and allocation of the deductions with respect to sources of income within and without the United States shall be determined as provided in section 119, under rules and regulations prescribed by the Commissioner with the approval of the Secretary.

(b) *Losses.*—(1) The deduction, for losses not connected with the trade or business if incurred in transactions entered into for profit, allowed by section 23 (e) (2) shall be allowed whether or not connected with income from sources within the United States, but only if the profit, if such transaction had resulted in a profit, would be taxable under this title.

(2) The deduction for losses of property not connected with the trade or business if arising from certain casualties or theft, allowed by section 23 (e) (3), shall be allowed whether or not connected with income from sources within the United States, but only if the loss is of property within the United States.

(c) *Charitable, etc., contributions.*—The so-called "charitable contribution" deduction allowed by section 23 (o) shall be allowed whether or not connected with income from sources within the United States, but only as to contributions or gifts made to domestic corporations, or to community chests, funds, or foundations, created in the United States, or to the vocational rehabilitation fund.

ART. 213–1. *Deductions allowed nonresident alien individuals—(a) No United States business or office.*—(1) *General rule.*—In general, a nonresident alien individual not engaged in trade or

ject to the provisions of section 211 (a) or 211 (c), as the case may be, depending on whether in the taxable year he derives fixed or determinable annual or periodical income from sources within the United States of more than $21,600, if he is not otherwise engaged in trade or business within the United States and has no office or place of business therein. A nonresident alien individual who is a member of a partnership which at any time within the taxable year is engaged in trade or business within the United States or has an office or place of business therein is considered as being engaged in trade or business within the United States or as having an office or place of business therein and is therefore taxable under section 211 (b). For definition of what the term "partnership" includes see section 901 (a) (3). The test of whether a partnership is engaged in trade or business within the United States, or has an office or place of business therein, is the same as in the case of a nonresident alien individual. (See article 211–7.)

CHAPTER XXVII

Foreign Corporations

Supplement I—Foreign Corporations

SEC. 231. *Tax on foreign corporations.*—(a) *Nonresident corporations.*—There shall be levied, collected, and paid for each taxable year, in lieu of the tax imposed by sections 13 and 14, upon the amount received by every foreign corporation not engaged in trade or business within the United States and not having an office or place of business therein, from sources within the United States as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable annual or periodical gains, profits, and income, a tax of 15 per centum of such amount, except that in the case of dividends the rate shall be 10 per centum, and except that in the case of corporations organized under the laws of a contiguous country such rate of 10 per centum with respect to dividends shall be reduced to such rate (not less than 5 per centum) as may be provided by treaty with such country. For inclusion in computation of tax of amount specified in shareholder's consent, see section 28.

(b) *Resident corporations.*—A foreign corporation engaged in trade or business within the United States or having an office or place of business therein shall be taxable as provided in section 14 (e) (1).

(c) *Gross income.*—In the case of a foreign corporation gross income includes only the gross income from sources within the United States.

(d) *Ships under foreign flag.*—The income of a foreign corporation, which consists exclusively of earnings derived from the operation of a ship or ships documented under the laws of a foreign country which grants an equivalent exemption to citizens of the United States and to corporations organized in the United States, shall not be included in gross income and shall be exempt from taxation under this title.

ART. 231–1. *Taxation of foreign corporations.*—For the purposes of this article and articles 231–2, 232–1, 235–1, 235–2, and 236–1, foreign corporations are divided into two classes: (a) foreign corporations not engaged in trade or business within the United States and not having an office or place of business therein at any time within the taxable year, referred to in the regulations as nonresident foreign corporations (see article 901–8); and (b) foreign corporations which at any time within the taxable year are engaged in trade or business within the United States or have an office or place of business therein, referred to in the regulations as resident foreign corporations (see article 901–8).

(a) *Nonresident foreign corporations.*—A nonresident foreign corporation is liable to the tax upon the amount received from sources within the United States, determined under the provisions of section 119, which is fixed or determinable annual or periodical gains, profits, and income. For the purposes of section 231 (a), the term "amount received" means "gross income." Specific items of fixed or determinable annual or periodical income are enumerated in the Act as interest (except interest on deposits with persons carrying on the banking business), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, but other fixed or determinable annual or periodical gains, profits, and income are also subject to the tax, as, for instance, royalties. As to the definition of fixed or determinable annual or periodical income see article 143–2. The items of fixed or determinable annual or periodical income from sources within the United States received by a corporation organized under the laws of France, which are exempt from Federal income tax under the provisions of the convention and protocol between the United States and France signed April 27, 1932, and effective January 1, 1936, are described in article 143–3.

The fixed or determinable annual or periodical income from sources within the United States, including royalties, but excluding dividends, of a nonresident foreign corporation is taxable at the rate of 15 percent. Dividends which are treated as income from sources within the United States are taxable at the rate of 10 percent, except that in the case of a nonresident foreign corporation organized under the laws of a contiguous country, such rate of 10 percent shall be reduced to such rate (not less than 5 percent) as may be provided by treaty with such country.

(b) *Resident foreign corporations.*—A resident foreign corporation is not taxable at the rate of 15 percent upon the items of fixed or determinable annual or periodical income enumerated in section 231 (a). A resident foreign corporation is liable to a tax of 19 percent upon its special class net income, that is, its net income from sources within the United States (gross income from sources within the United States minus the statutory deductions provided in sections 23 and 232) less the credits allowed against net income by section 26 (a) and (b). (See section 14 (a).)

As used in section 231, section 119, section 143, section 144, and section 211, the phrase "engaged in trade or business within the United States" includes the performance of personal services within the United States at any time within the taxable year. Such phrase does not include the effecting of transactions in the United States in stocks, securities, or commodities (including hedging transactions) through a resident broker, commission agent, or custodian.

Whether a foreign corporation has an "office or place of business" within the United States depends upon the facts in a particular case. The term "office or place of business," however, implies a place for the regular transaction of business and does not include a place where casual or incidental transactions might be, or are, effected.

ART. 231–2. *Gross income of foreign corporations.*—In the case of a foreign corporation, including a life insurance company not carrying on an insurance business within the United States and holding no reserve funds upon business transacted within the United States (see section 201 (b) (3)), an insurance company other than life or mutual not carrying on an insurance business within the United States (see section 204 (a) (3)) and a mutual insurance company other than life not carrying on an insurance business within the United States (see section 207 (a)), the term "gross income" means gross income from sources within the United States as defined and described in section 119. (See articles 119–1 to 119–14.) The items of gross income from sources without the United States and therefore not taxable to foreign corporations are described in section 119 (c). As to the definition of a foreign corporation see section 901 (a) (2) and (5). As to foreign life insurance companies, see article 201 (b)–2. As to foreign corporations formed or availed of to avoid surtax see article 102–4. As to personal holding companies organized under the laws of foreign countries, see article 406–1. As to foreign personal holding companies, see Chapter XXXIV.

(a) *Nonresident foreign corporations.*—A nonresident foreign corporation is taxable under section 231 (a) only on fixed or determinable annual or periodical gross income received from sources within the United States. Its taxable income does not include profits derived from the effecting of transactions in the United States in stocks, securities, or commodities (including hedging transactions) through a resident broker, commission agent, or custodian, or profits derived from the sale within the United States of personal property or real property located therein.

(b) *Resident foreign corporations.*—The gross income from sources within the United States of a resident foreign corporation is not limited to the items of fixed or determinable annual or periodical income referred to in section 231

(a), but includes every item of gross income which is treated as income from sources within the United States, except those items which are specifically exempt from taxation by statute or treaty or which are not taxable by the Federal Government under the Constitution. (See sections 22 (b), 119, and 231 (d).)

A foreign corporation which effects transactions in the United States in stocks, securities, or commodities (including hedging transactions) through a resident broker, commission agent, or custodian is not merely by reason of such transactions considered as being engaged in trade or business within the United States which would cause it to be classed as a resident foreign corporation. However, a foreign corporation which at any time within the taxable year is otherwise engaged in trade or business in the United States or has an office or place of business therein, being a resident foreign corporation, is taxable upon all income derived from sources within the United States, including the profits realized from such transactions. A resident foreign corporation is also required to include in its gross income capital gains, gains from hedging transactions, and profits derived from the sale within the United States of personal property, or of real property located therein.

ART. 231–3. *Exclusion of earnings of foreign ships from gross income.*—A resident foreign corporation may exclude from gross income under section 231 (d) so much of its income from sources within the United States as consists of earnings derived from the operation of a ship or ships documented under the laws of a foreign country, to the same extent as provided in article 212–2 with respect to nonresident alien individuals.

A nonresident foreign corporation is not required to include in gross income such income from sources within the United States as is derived from the operation of a ship or ships, whether or not the foreign country under the laws of which such ships are documented meets the equivalent exemption requirements of the statute.

SEC. 232. *Deductions.*—(a) *In general.*—In the case of a foreign corporation the deductions shall be allowed only if and to the extent that they are connected with income from sources within the United States; and the proper apportionment and allocation of the deductions with respect to sources within and without the United States shall be determined as provided in section 119, under rules and regulations prescribed by the Commissioner with the approval of the Secretary.

(b) *Charitable, and so forth, contributions.*—The so-called "charitable contribution" deduction allowed by section 23 (q) shall be allowed whether or not connected with income from sources within the United States.

ART. 232–1. *Deductions allowed foreign corporations.*—(a) *Nonresident foreign corporations.*—A nonresident foreign corporation is not allowed any deductions from gross income from sources within the United States, the tax being imposed upon the amount of gross income received. (See article 231–1.)

(b) *Resident foreign corporations.*—A resident foreign corporation is allowed the same deductions from its gross income arising from sources within the United States as are allowed a domestic corporation under section 23 to the extent that such deductions are connected with such gross income, except that the so-called charitable contribution deduction allowed by section 23 (q) is allowed whether or not connected with income from sources within the United States. The proper apportionment and allocation of the deductions with respect to sources within and without the United States shall be determined as provided in section 119. As to foreign life insurance companies, see article 201 (b)–2. As to foreign corporations formed or availed of to avoid surtax, see article 102–4. As to personal holding companies organized under the laws of foreign countries, see article 406–1. As to foreign personal holding companies, see Chapter XXXIV.

SEC. 233. *Allowance of deductions and credits.*—A foreign corporation shall receive the benefit of the deductions and credits allowed to it in this title only by filing or causing to be filed with the collector a true and accurate return of its total income received from all sources in the United States, in the manner prescribed in this title; including therein all the information which the Commissioner may deem necessary for the calculation of such deductions and credits.

ART. 233–1. *Allowance of deductions and credits.*—The benefit of the deductions and credits allowed a resident foreign corporation can be had only by filing or causing to be filed with the collector a true and accurate return of its total income received from sources within the United States. Only items of interest and dividends included in gross income may be credited under section 26 (a) and (b). Inasmuch as a nonresident foreign corporation is taxable under section 231 (a) only upon fixed or determinable annual or periodical gross income received from sources within the United States, such foreign corporation may not receive the benefit of the deductions and credits by filing a return of income.

SEC. 234. *Credits against tax.*—Foreign corporations shall not be allowed the credits against the tax for taxes of foreign countries and possessions of the United States allowed by section 131.

SEC. 235. *Returns.*—(a) *Time of filing.*—In the case of a foreign corporation not having any office or place of business in the United States the return, in lieu of the time prescribed in section 53 (a) (1), shall be made on or before the fifteenth day of the sixth month following the close of the fiscal year, or, if the return is made on the basis of the calendar year then on or before the fifteenth day of June. If any foreign corporation has no office or place of business in the United States but has an agent in the United States, the return shall be made by the agent.

(b) *Exemption from requirement.*—Subject to such conditions, limitations, and exceptions and under such regulations as may be prescribed by the Commissioner, with the approval of the Secretary, corporations subject to the tax imposed by section 231 (a) may be exempted from the requirement of filing returns of such tax.

ART. 235–1. *Time and place for filing returns of foreign corporations.*—(a) *Nonresident foreign corporations.*—The return in the case of a nonresident foreign corporation must be made on or before the 15th day of the sixth month following the close of the fiscal year, or, if the return is made on the basis of a calendar year then on or before the 15th day of June. If a nonresident foreign corporation has an agent in the United States, the return shall be made by the agent. The return must be filed with the collector of internal revenue, Baltimore, Md. (See section 53 (b) (2).) For failure to make and file a return within the time prescribed, see section 291. For cases in which no return is required see paragraph (a) of article 235–2.

(b) *Resident foreign corporations.*—The return in the case of a resident foreign corporation, in lieu of the time prescribed in section 235, shall be made on or before the 15th day of the third month following the close of the fiscal year, or on or before the 15th day of March if on the basis of the calendar year. (See section 53 (a) (1).) The return must be filed with the collector of internal revenue for the district in which the resident foreign corporation has its principal place of business or principal office or agency in the United States. (See section 53 (b) (2).) For failure to make and file a return within the time prescribed see section 291.

ART. 235–2. *Return of income.*—(a) *Nonresident foreign corporations.*—If the tax liability of a nonresident foreign corporation is fully satisfied at the source a return of income is not required. A nonresident foreign corporation shall make or have made a return on Form 1120NB with respect to that portion of its income received from sources within the United States consisting of interest on so-called tax-free covenant bonds on which a tax of only 2 percent was withheld at the source, and with respect to any other fixed or determinable annual or periodical income upon which the tax was not fully satisfied at the source, including dividends received from a foreign corporation which are treated as income from sources within the United States under section 119 (a) (2) (B), and shall pay the balance of the tax shown to be due.

(b) *Resident foreign corporations.*—If a foreign corporation at any time within the taxable year is a resident corporation it shall make a full and accurate return on Form 1120 of its income received from sources within the United States.

SEC. 236. *Payment of tax.*—(a) *Time of payment.*—In the case of a foreign corporation not having any office or place of business in the United States the total amount of tax imposed by this title shall be