

work in France. Q's sole function is to act as a courier to deliver sales documents to customers in France. With respect to Q's activities in France, a separate set of books and records as described in paragraph (d) is maintained. Under paragraph (c) of this section, Q's activities in France do not constitute a QBU since they are merely ancillary to W's manufacturing and selling business. Q is not considered to have a QBU because an individual's activities as an employee are not considered to constitute a trade or business of the individual under paragraph (c).

*Example 4.* The facts are the same as in example (3) except that the courier function is the sole activity of a wholly-owned French subsidiary of W. Under paragraph (b)(2)(i) of this section, the French subsidiary is considered to be a QBU.

*Example 5.* A corporation incorporated in the Netherlands is a subsidiary of a domestic corporation and a holding company for the stock of one or more subsidiaries incorporated in other countries. The Dutch corporation's activities are limited to paying its directors and its administrative expenses, receiving capital contributions from its United States parent corporation, contributing capital to its subsidiaries, receiving dividend distributions from its subsidiaries, and distributing dividends to its domestic parent corporation. Under paragraph (b)(2)(i) of this section, the Netherlands corporation is considered to be a QBU.

*Example 6.* Taxpayer A, an individual resident of the United States, is engaged in a trade or business wholly unrelated to any type of investment activity. A also maintains a portfolio of foreign currency-denominated investments through a foreign broker. The broker is responsible for all activities necessary to the management of A's investments and maintains books and records as described in paragraph (d) of this section, with respect to all investment activities of A. A's investment activities qualify as a QBU under paragraph (b)(2)(ii) of this section to the extent the activities engaged in by A generate expenses that are deductible under section 212 (other than that part of section 212 dealing with expenses incurred in connection with taxes).

*Example 7.* Taxpayer A, an individual resident of the United States, is the sole shareholder of foreign corporation (FC) whose activities are limited to trading in stocks and securities. FC is a QBU under paragraph (b)(2)(i) of this section.

*Example 8.* Taxpayer A, an individual resident of the United States, markets and sells in Spain and in the United States various products produced by other United States manufacturers. A has an office and employs a salesman to manage A's activities in Spain, maintains a separate set of books and records with respect to his activities in Spain, and is engaged in a trade or business

as defined in paragraph (c) of this section. Therefore, under paragraph (b)(2)(ii) of this section, the activities of A in Spain are considered to be a QBU.

*Example 9.* Foreign corporation FX is incorporated in Mexico and is wholly owned by a domestic corporation. The domestic corporation elects to treat FX as a domestic corporation under section 1504(d). FX operates entirely in Mexico and maintains a separate set of books and records with respect to its activities in Mexico. FX is a QBU under paragraph (b)(2)(i) of this section. The activities of FX in Mexico also constitute a QBU under paragraph (b)(2)(ii) of this section.

*Example 10.* F, a foreign corporation, computes a gain of \$100 from the disposition of a United States real property interest (as defined in section 897(c)). The gain is taken into account as if F were engaged in a trade or business in the United States and as if such gain were effectively connected with such trade or business. F is a QBU under paragraph (b)(2)(i) of this section because of its corporate status. F's disposition activity constitutes a separate QBU under paragraph (b)(3) of this section.

[T.D. 8279, 55 FR 284, Jan. 4, 1990]

#### § 1.989(b)-1 Definition of weighted average exchange rate.

For purposes of section 989(b)(3) and (4), the term "weighted average exchange rate" means the simple average of the daily exchange rates (determined by reference to a qualified source of exchange rates within the meaning of § 1.964-1(d)(5)), excluding weekends, holidays and any other non-business days for the taxable year.

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#### § 1.989(c)-1 Transition rules for certain branches of United States persons using a net worth method of accounting for taxable years beginning before January 1, 1987.

(a) *Applicability*—(1) *In general.* This section applies to qualified business units (QBU) branches of United States persons, whose functional currency (as defined in section 985 of the Code and regulations issued thereunder) is other than the United States dollar (dollar) and that used a net worth method of accounting for their last taxable year beginning before January 1, 1987. Generally, a net worth method of accounting is any method of accounting under

which the taxpayer calculates the taxable income of a QBU branch based on the net change in the dollar value of the QBU branch's equity over the course of a taxable year, taking into account any remittance made during the year. QBU branch equity is the excess of QBU branch assets over QBU branch liabilities. For all taxable years beginning after December 31, 1986, such QBU branches must use the profit and loss method of accounting as described in section 987, except to the extent otherwise provided in regulations under section 985 or any other provision of the Code.

(2) *Insolvent QBU branches.* A taxpayer may apply the principles of this section to a QBU branch that used a net worth method of accounting for its last taxable year beginning before January 1, 1987, whose \$E pool (as defined in paragraph (d)(3)(i) of this section) is negative. For taxable years beginning on or after October 25, 1991, the principles of this section shall apply to insolvent QBU branches.

(b) *General rules.* For the general rules, see § 1.987-5(b).

(c) *Determining the pool(s) from which a remittance is made.* To determine from which pool(s) a remittance is made, see § 1.987-5(c).

(d) *Calculation of section 987 gain or loss—(1) In general.* See § 1.987-5(d)(1) for rules to make this calculation.

(2) *Step 1—Calculate the amount of the functional currency pools.* For calculation of the amount of the functional currency pools, see § 1.987-5(d)(2).

(3) *Step 2—Calculate the dollar basis pools—(i) Dollar basis of the EQ pool—(A) Beginning dollar basis.* The beginning dollar basis of the EQ pool (hereinafter referred to as the \$E pool) equals the final net worth of the QBU branch. Final net worth of the QBU branch equals the QBU branch's equity value (assets less liabilities) measured in dollars at the end of the taxpayer's last taxable year beginning before January 1, 1987, determined on the basis of the QBU branch's books and records as adjusted according to United States tax principles.

(B) *Adjusting the \$E pool.* For adjustments to be made to the \$E pool, see § 1.987-5(d)(3)(i)(B).

(ii) *Dollar basis of the post-86 profits pool.* To calculate the dollar basis of the post-86 profits pool, see § 1.987-5(d)(3)(ii).

(iii) *Dollar basis of the equity pool.* To calculate the dollar basis of the equity pool, see § 1.987-5(d)(3)(iii).

(4) *Step 3—Calculation of the dollar basis of a remittance.* To calculate the dollar basis of the EQ remitted, see § 1.987-5(d)(4).

(5) *Step 4—Calculation of the section 987 gain or loss on a remittance.* To calculate 987 gain or loss determined on a remittance, see § 1.987-5(d)(5).

(e) *Functional currency adjusted basis of QBU branch assets acquired in taxable years beginning before January 1, 1987.* To determine the functional currency adjusted basis of QBU branch assets acquired in taxable years beginning before January 1, 1987, see § 1.987-5(e).

(f) *Functional currency amount of QBU branch liabilities acquired in taxable years beginning before January 1, 1987.* To determine the functional currency amount of QBU branch liabilities acquired in taxable years beginning before January 1, 1987, see § 1.987-5(f).

[T.D. 8367, 56 FR 48437, Sept. 25, 1991]

DOMESTIC INTERNATIONAL SALES  
CORPORATIONS

**§ 1.991-1 Taxation of a domestic international sales corporation.**

(a) *In general.* A corporation which is a DISC for a taxable year is not subject to any tax imposed by subtitle A of the Code (sections 1 through 1564) for such taxable year, except for the tax imposed by chapter 5 thereof (sections 1491 through 1494) on certain transfers to avoid tax. Thus, for example, a corporation which is a DISC for a taxable year is not subject for such year to the corporate income tax (section 11), the minimum tax on tax preferences (sections 56 through 58), or the accumulated earnings tax (sections 531 through 537). A DISC is liable for the payment of all taxes payable by corporations under other subtitles of the Code, such as, for example, income taxes withheld at the source and other employment taxes under subtitle C and the interest equalization tax and other miscellaneous excise taxes imposed by