

Internal Revenue Service, Treasury

§ 1.861-1

in exchange for regular and residual interests over any period of 10 consecutive days and the REMIC may designate any one of those 10 days as its startup day. The day so designated is then the startup day, and all interests are treated as issued on that day.

[T.D. 8458, 57 FR 61309, Dec. 24, 1992; 58 FR 8098, Feb. 11, 1993]

§ 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) [Reserved]

[T.D. 8458, 57 FR 61313, Dec. 24, 1992]

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 ratable 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.

(c) *Computation of income.* If a taxpayer has gross income from sources within or without the United States,

together with gross income derived partly from sources within and partly from sources without the United States, the amounts thereof, together with the expenses and investment applicable thereto, shall be segregated; and the taxable income from sources within the United States shall be separately computed therefrom.

[T.D. 6500, 25 FR 11910, Nov. 26, 1960, as amended by T.D. 7928, 48 FR 55845, Dec. 16, 1983]

§ 1.861-2 Interest.

(a) *In general.* (1) Gross income consisting of interest from the United States or any agency or instrumentality thereof (other than a possession of the United States or an agency or instrumentality of a possession), a State or any political subdivision thereof, or the District of Columbia, and interest from a resident of the United States on a bond, note, or other interest-bearing obligation issued, assumed or incurred by such person shall be treated as income from sources within the United States. Thus, for example, income from sources within the United States includes interest received on any refund of income tax imposed by the United States, a State or any political subdivision thereof, or the District of Columbia. Interest other than that described in this paragraph is not to be treated as income from sources within the United States. See paragraph (a)(7) of this section for special rules concerning substitute interest paid or accrued pursuant to a securities lending transaction.

(2) The term "resident of the United States", as used in this paragraph, includes (i) an individual who at the time of payment of the interest is a resident of the United States, (ii) a domestic corporation, (iii) a domestic partnership which at any time during its taxable year is engaged in trade or business in the United States, or (iv) a foreign corporation or a foreign partnership, which at any time during its taxable year is engaged in trade or business in the United States.

(3) The method by which, or the place where, payment of the interest is made is immaterial in determining whether interest is derived from sources within the United States.