change, or otherwise deal with or dispose of the trust property or income for less than an adequate and full consideration in money or money's worth, or is authorized to lend the trust property or income to the grantor without adequate interest. On the other hand, such authority may be indicated by the actual administration of the trust.

(f) *Limitations of section.* Despite the limitations of this section, the grantor of a trust directing the payment or application of the income therefrom in satisfaction of the grantor's legal obligations shall continue to be taxable on the income. The grantor may also be taxable on the income of a trust on the ground that such income is attributable to him in a capacity unrelated to dominion and control over the trust as such as defined in paragraphs (c) (d) and (e) of this section. Thus, the provisions of this section do not affect the principles governing the taxability of future income to the assignor thereof whether or not the assignment is by means of a trust. Nor, for example, do the provisions of this section affect the applicability of section 22 (a) to the creator of a family partnership. See also sections 166 and 167.

§ 39.22 (a)–22 *Trust income taxable to person other than grantor* Where a person other than the grantor of property transferred in trust has a power exercisable solely by himself to vest the corpus or the income therefrom in himself, the income therefrom shall be included in computing the net income of such person. Even though such a power has been partially released or otherwise modified so that the person holding it can no longer vest the corpus or the income of the trust in himself, the income shall continue to be taxable to such person, if after such release or modification, he has retained such control of the trust as would, within the principles of § 39.22 (a)–21, subject a grantor of such a trust to tax on the income thereof. This section shall not apply with respect to a power over income, as originally granted or thereafter modified, if the grantor is otherwise taxable under § 39.22 (a)–21. See also § 39.166–1.

§ 39.22 (a)–23 *Allocations by cooperative associations; tax treatment as to patrons*—(a) *In general.* Amounts allocated on the basis of the business done with or for a patron by a cooperative association, whether or not entitled to tax treatment under section 101 (12) (B) in cash, merchandise, capital stock, revolving-fund certificates, retain certificates, certificates of indebtedness, letters of advice or in some other manner disclosing to the patron the dollar amount allocated shall be included in the computation of the gross income of such patron for the taxable year in which received to the extent prescribed in paragraph (b) of this section, regardless of whether the amount allocated is deemed, for the purpose of section 101 (12) (B) to be made at the close of a preceding taxable year of the cooperative association. The determination of the extent of taxability of such amounts is in no way dependent upon the method of accounting employed by the patron or upon the basis, cash, accrual or otherwise, upon which the net income of such patron is computed.

(b) *Extent of taxability.* (1) Amounts allocated to a patron on a patronage basis by a cooperative association with respect to products marketed for such patron, or with respect to supplies, equipment, or services the cost of which was deductible by the patron under section 23, shall be included in the computation of the gross income of such patron to the following extent:

(i) If the allocation is in cash, in the amount of cash received.

(ii) If the allocation is in merchandise, to the extent of the fair market value of such merchandise at the time of receipt by the patron.

(iii) If the allocation is in the form of capital stock, revolving fund certificates, certificates of indebtedness, letters of advice, retain certificates or similar documents—

(*a*) To the extent of the face amount of such documents, if the allocation was made in fulfillment and satisfaction of a valid obligation of such association to the patron, which obligation was in existence prior to the receipt by the cooperative association of the amount allocated. For this purpose, it is immaterial whether such allocation was made within the time required by § 39.101 (12)–4 (a) (2)

(*b*) To the extent of the face amount of such documents, if the allocation was made with respect to patronage of a year preceding the taxable year from amounts retained as "reasonable reserves" under § 39.101–4 (a).

(*c*) To the extent of the cash or merchandise received in redemption or satisfaction of such documents (except those which are negotiable instruments) at the time of receipt of such cash or merchandise by the patron, where such allocation was not made in pursuance of the valid obligation referred to in subdivision (*a*) of this subparagraph, or from amounts retained as "reasonable reserves" under § 39.101 (12)–4 (a), referred to in subdivision (*b*) of this subparagraph. Where, in such case, the documents allocated are negotiable instruments, such documents shall be includible in the income of the patron to the extent of their fair market value at the time of their receipt.

(2) Amounts which are allocated on a patronage basis by a cooperative association with respect to supplies, equipment, or services the cost of which was not deductible by the patron under section 23, are not includible in the computation of the gross income of such patron; however, in the case of such amounts which are allocated with respect to capital assets (as defined in section 117 (a) (1)) or property used in the trade or business within the meaning of section 117 (j), shall, to the extent set forth in subdivisions (i), (ii) and (iii) of subparagraph (1) of this paragraph, be taken into account in determining under section 113 the cost or other basis of the assets or property purchased for the patron.

§ 39.22 (b) *Statutory provisions; exclusions from gross income.*

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 chapter: * * *

§ 39.22 (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 may be excluded from gross income except (a) those items of income which are under the Constitution, not taxable by the Federal Government; (b) those items of income which are exempt from tax on income under the provisions of any act of Congress still in effect; and (c) the income excluded under the provisions of the Internal Revenue Code (see particularly 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 Internal Revenue Code to be made from gross income in computing net income. As to other items not to be included in gross income, see sections 22 (b) 112, 119, 127 (c), 165, and 171 and Supplements G, H, I, and J (sections 201 to 252, inclusive) Section 607 (h) of the Merchant Marine Act, 1936, as amended, (46 U. S. C. 1177 (h)) reads as follows:

(h) The earnings of any contractor receiving an operating-differential subsidy under authority of this act, which are deposited in the contractor's reserve funds as provided in this section, except earnings withdrawn from the special reserve funds and paid into the contractor's general funds or distributed as dividends or bonuses as provided in paragraph 4 of subsection (c) of this section, shall be exempt from all Federal taxes. Earnings withdrawn from such special reserve fund shall be taxable as if earned during the year of withdrawal from such fund.

§ 39.22 (b) (1) *Statutory provisions; exclusions from gross income; life insurance.*

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 chapter:

(1) *Life insurance, etc., amounts received:*

(A) Under a life insurance contract, paid by reason of the death of the insured; or

(B) Under a contract of an employer providing for the payment of such amounts to the beneficiaries of an employee, paid by reason of the death of the employee;

whether in a single sum or otherwise (but if such amounts are held by the insurer, or the employer, under an agreement to pay interest thereon, the interest payments shall be included in gross income). The aggregate of the amounts excludible under subparagraph (B) by all the beneficiaries of the employee under all such contracts of any one employer may not exceed $5,000.

[Sec. 22 (b) (1) as amended by sec. 302 (a), Rev. Act 1951]

§ 39.22 (b) (1)–1 *Life insurance; amounts paid by reason of the death of the insured.* The proceeds of life insur-

(1) Earnings or profits accumulated since February 28, 1913, or

(2) Earnings or profits of the taxable year computed without regard to the amount of the earnings or profits (whether of such year or accumulated since February 28, 1913) at the time the distribution was made.

The earnings or profits of the taxable year shall be computed as of the close of such year, without diminution by reason of any distributions made during the taxable year. For the purpose of determining whether a distribution constitutes a dividend, it is unnecessary to ascertain the amount of the earnings and profits accumulated since February 28, 1913, if the earnings and profits of the taxable year are equal to or in excess of the total amount of the distributions made within such year.

(b) In the case of a corporation which, under the law applicable to the taxable year in which a distribution is made, is a personal holding company or which, for the taxable year in respect of which a distribution is made under section 504 (c) relating to dividends paid within 2½ months after the close of the taxable year, or section 506, relating to deficiency dividends, or corresponding provisions of a prior income-tax law, was under the applicable law a personal holding company, the term "dividend," in addition to the meaning set forth in the first sentence of section 115 (a) also means a distribution to its shareholders as follows: A distribution within a taxable year of the corporation, or of a shareholder, is a dividend to the extent of the corporation's subchapter A net income less the sum of the net operating loss credit provided in section 26 (c) (1) the dividend carry-over provided in section 27 (c) and the deduction for amounts for retirement of indebtedness provided in section 504 (b) for the taxable year in which, or, in the case of a distribution under section 504 (c) or section 506, the taxable year in respect of which, the distribution is made.

(c) The term "dividend" does not include distributions under section 115 (c) relating to distributions in liquidation, section 115 (e) relating to distributions by personal service corporations, or section 115 (f) relating to stock dividends, or certain distributions by insurance companies. In all other cases the term includes any distribution to shareholders to the extent made out of accumulated or current earnings or profits.

(d) A taxable distribution made by a corporation to its shareholders shall be included in the gross income of the distributees when the cash or other property is unqualifiedly made subject to their demands.

(e) The application of section 115 (a) may be illustrated by the following examples:

Example (1). At the beginning of the calendar year 1952, the M Corporation had an operating deficit of $200,000 and the earnings or profits for the year amounted to $100,000. Beginning on March 16, 1952, the corporation made quarterly distributions of $25,000 during the taxable year to its shareholders. Each distribution is a taxable dividend in full, irrespective of the actual or the pro rata amount of the earnings or profits on hand at any of the dates of distribution, since the total distributions made during the year ($100,000) did not exceed the total earnings or profits of the year ($100,000).

Example (2). At the beginning of the calendar year 1952, the N Corporation, a personal holding company, had no accumulated earnings or profits. During that year it made no earnings or profits but its subchapter A net income, due to the disallowance of certain deductions, was $16,000. It distributed to shareholders on December 15, 1952, $15,000, and on February 1, 1953, $1,000, the latter amount being claimed as a deduction under section 504 (c) in its personal holding company return for 1952 filed on March 15, 1953. Both distributions are taxable dividends in full, since they do not exceed the subchapter A net income for 1952, the taxable year in which the distribution of $15,000 was made and with respect to which the distribution of $1,000 was made. It is immaterial whether the N Corporation is a personal holding company for the taxable year 1953 or whether it had any income for that year.

Example (3). In 1952, a deficiency in personal holding company tax was established against the O Corporation for the taxable year 1948 in the amount of $35,500 based on an undistributed subchapter A net income of $42,000 which consisted of a subchapter A net income of $52,000 minus a deduction of $10,000 for amounts used for retirement of indebtedness provided in section 504 (b). The O Corporation complied with the provisions of section 506 and in December 1952 distributed $42,000 to its stockholders as "deficiency dividends." The distribution of $42,000 is a taxable dividend since it does not exceed $42,000 (subchapter A net income of $52,000 for 1948, the taxable year with respect to which the distribution was made, minus the deduction for retirement of indebtedness of $10,000). It is immaterial whether the O Corporation is a personal holding company for the taxable year 1952 or whether it had any income for that year.

Example (4). At the beginning of the taxable year 1952, the P Corporation, a personal holding company, had a deficit in earnings and profits of $200,000. During that year it made earnings and profits of $55,000. For that year, however, it had a subchapter A net income of $100,000, a net operating loss credit under section 26 (c) (1) of $10,000 and a deduction for retirement of indebtedness under section 504 (b) of $10,000. During such taxable year it distributed to its shareholders $100,000. The distribution of $100,000 is a taxable dividend to the extent of $80,000 (subchapter A net income of $100,000 minus the net operating loss credit of $10,000 and the deduction for retirement of indebtedness of $10,000). No interest shall be allowed or paid in respect of any overpayment of tax resulting from the inclusion in taxable income by any shareholder of his proportionate share of the distribution of $100,000.

Example (5). If the facts were the same as in example (4) except that the P Corporation had earnings and profits for the taxable year 1952 of $90,000, the distribution of $100,000 would be a taxable dividend to the extent of $90,000 since its earnings and profits for that year, $90,000, exceed $80,000 (subchapter A net income of $100,000 minus the net operating loss credit of $10,000 and the deduction for retirement of indebtedness of $10,000).

§ 39.115 (a)–2 *Earnings or profits.* (a) In determining the amount of earnings or profits (whether of the taxable year, or accumulated since February 28, 1913, or accumulated before March 1, 1913) due consideration must be given to the facts, and, while mere bookkeeping entries increasing or decreasing surplus will not be conclusive, the amount of the earnings or profits in any case will be dependent upon the method of accounting properly employed in computing net income. For instance, a corporation keeping its books and filing its income tax returns under sections 41, 42, and 43 on the cash receipts and disbursements basis may not use the accrual basis in determining earnings and profits; a corporation computing income on the installment basis as provided in section 44 shall, with respect to the installment transactions, compute earnings and profits on such basis; and an insurance company subject to taxation under section 204 shall exclude from earnings and profits that portion of any premium which is unearned under the provisions of section 204 (b) (5) and which is segregated accordingly in the unearned premium reserve.

(b) 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) or corresponding provisions of prior Revenue Acts. Gains and losses within the purview of section 112 or corresponding provisions of prior Revenue Acts are brought into the earnings and profits at the time and to the extent such gains and losses are recognized under that section (see § 39.115 (e)–1) 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.

(c) (1) In the case of a corporation in which depletion or depreciation is a factor in the determination of income, the only depletion or depreciation deductions to be considered in the computation of the total earnings and profits are those based on cost or other basis without regard to March 1, 1913, value. In computing the earnings and profits for any period beginning after February 28, 1913, the only depletion or depreciation deductions to be considered are those based on (i) costs or other basis, if the depletable or depreciable asset was acquired subsequent to February 28, 1913, or (ii) adjusted cost or March 1, 1913, value, whichever is higher, if acquired before March 1, 1913. Thus, discovery or percentage depletion under all Revenue Acts for mines and oil and gas wells is not to be taken into consideration in computing the earnings and profits of a corporation. Similarly, where the basis of property in the hands of a corporation is a substituted basis, such basis, and not the fair market value of the property at the time of the acquisition by the corporation, is the basis for computing depletion and depreciation for the purpose of determining earnings and profits of the corporation.

(2) The application of subparagraph (1) of this paragraph may be illustrated by the following example:

puted under sections 11 and 12, or in the alternative under section 117 (c), shall in no case be less than 30 percent of the amount which is the sum of the aggregate of the gross amounts of fixed or determinable annual or periodical income from sources within the United States plus the amount, determined in accordance with the provisions of section 211 (a) (1) (B) and of paragraph (b) (2) of this section, by which gains from sales or exchanges of capital assets exceed losses from such sales or exchanges.

(d) *United States business.* A nonresident alien individual within class (3), referred to in paragraph (a) of this section, is not taxable at the rate of 30 percent upon the items of gross income enumerated in section 211 (a) The net income from sources within the United States of such a nonresident alien individual (gross income from sources within the United States minus the statutory deductions provided in sections 23 and 213) less the credits against net income allowable to an individual by section 25, is subject to the normal tax and surtax under sections 11 and 12.

(e) *What constitutes engaging in trade or business.* As used in sections 119, 143, 144, 211, and 231, 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 but does not include the performance of personal services 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 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. See also § 39.212–1. As used in section 211 (b) the term "commodities" means only goods of a kind customarily dealt in on an organized commodity exchange, such as a grain futures or a cotton futures market, and does not include merchandise in the ordinary channels of commerce. 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 merely because the trustee is engaged in trade or business in the United States.

§ 39.212 *Statutory provisions; nonresident alien individuals; gross income.*

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) *Exclusions.* The following items shall not be included in gross income of a nonresident alien individual and shall be exempt from taxation under this chapter:

(1) *Ships under foreign flag.* 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;

(2) *Aircraft of foreign registry.* Earnings derived from the operation of aircraft registered 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.

[Sec. 212 as amended by sec. 1 (a), Pub. Law 514 (80th Cong.)]

§ 39.212–1 *Gross income of nonresident alien individuals*—(a) *In general.* (1) In general, in the case of nonresident alien individuals "gross income" means only the gross income from sources within the United States. See section 119 and the regulations thereunder. 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 §§ 39.211–2 to 39.211–6, inclusive.

(2) 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 before 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 before the close of the taxable year.

(b) *No United States business.* The gross income of a nonresident alien individual not engaged in trade or business within the United States 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 and any gain from the sale or exchange of a capital asset to the extent required to be included in gross income under the provisions of section 211 (a) (1) (B) or section 211 (c).

(c) *United States business.* 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 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).

(d) *What constitutes engaging in trade or business within United States.* (1) 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 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 or of international organizations, see section 116 (h)

(2) 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, 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. As used in section 211 (b), the term "commodities" means only goods of a kind customarily dealt in on an organized commodity exchange, such as a grain futures or a cotton futures market, and does not include merchandise in the ordinary channels of commerce.

§ 39.212–2 *Exclusion of earnings of foreign ships or aircraft from gross income*—(a) *Ships under foreign flag.* 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 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 paragraph. A nonresident alien individual not engaged in trade or business within the United States 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

or determinable annual or periodical gains, profits, and income, a tax of 30 per centum of such amount, except that in the case of corporations organized under the laws of any country in North, Central, or South America, or in the West Indies, or of Newfoundland such rate 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.

(2) *Cross reference.* 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 shall be taxable as provided in section 13 and section 15.

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

(d) *Exclusions.* The following items shall not be included in gross income of a foreign corporation and shall be exempt from taxation under this chapter:

(1) *Ships under foreign flag.* 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;

(2) *Aircraft of foreign registry.* Earnings derived from the operation of aircraft registered 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.

[Sec. 231 as amended by sec. 206, Rev. Act 1939; sec. 3 (c), Rev. Act 1940; secs. 104 (d), 106, and 109 (a), Rev. Act 1941; secs. 107 and 160 (d) and (e), Rev. Act 1942; sec. 1 (b), Pub. Law 514 (80th Cong.); sec. 121 (g) (5), Rev. Act 1950]

§ 39.231–1 *Taxation of foreign corporations*—(a) *General.* For the purposes of this section and §§ 39.231–2, 39.232–1, 39.235–1, 39.235–2, and 39.236–1, foreign corporations are divided into two classes: (1) Foreign corporations not engaged in trade or business within the United States at any time within the taxable year, referred to in the regulations as nonresident foreign corporations (see § 39.3797–3) and (2) foreign corporations which at any time within the taxable year are engaged in trade or business within the United States, referred to in the regulations as resident foreign corporations (see § 39.3797–3)

(b) *Nonresident foreign corporations.* (1) 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 Internal Revenue Code as interest (except interest on deposits with persons carrying on the banking business) dividends, rents, salaries, wages, premiums, annuities, compensations, renumerations, 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 § 39.143–2.

(2) The fixed or determinable annual or periodical income from sources within the United States, including royalties, of a nonresident foreign corporation is taxable at the rate of 30 percent. In the case of dividends received by a nonresident foreign corporation, the rate shall be reduced to such rate as may be provided by treaty with any country.

(c) *Resident foreign corporations.* (1) A resident foreign corporation is not taxable upon the items of fixed or determinable annual or periodical income enumerated in section 231 (a) at the rate specified in that section. A resident foreign corporation is, under section 13, liable to a tax of 30 percent (25 percent for taxable years beginning after March 31, 1954) of its normal-tax net income. The normal-tax net income of a resident foreign corporation 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 provided in section 26 (a) and (b)

(2) A resident foreign corporation is, under section 15, also liable to a tax of 22 percent of the amount of its corporation surtax net income in excess of $25,000. See, however, § 39.15–2, as to the circumstances under which the $25,000 exemption from surtax for certain taxable years may be disallowed in whole or in part. The corporation surtax net income of a resident foreign corporation 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 credit provided in section 26 (b) which credit is limited in amount to 85 percent of its adjusted net income from sources within the United States computed without regard to the deduction for net operating loss provided in section 23 (s)

(3) For taxable years beginning before April 1, 1954, and ending after March 31, 1954, see § 39.108–2.

(d) *Meaning of terms used.* As used in sections 119, 143, 144, 211, and 231, 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. The term "commodities," as used in section 211 (b) means only goods of a kind customarily dealt in on an organized commodity exchange, such as a grain futures or a cotton futures market, and does not include merchandise in the ordinary channels of commerce.

§ 39.231–2 *Gross income of foreign corporations*—(a) *In general.* 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 (a) (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 §§ 39.119 (a)–1 to 39.119(e)–4, inclusive. 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 3797 (a) (3) and (5). As to foreign life insurance companies, see § 39.201–2. As to foreign corporations formed or availed of to avoid surtax, see § 39.102–4. As to personal holding companies organized under the laws of foreign countries, see § 39.595–1. As to foreign personal holding companies, see sections 331 to 340, inclusive, and §§ 39.331–1 to 39.339–3, inclusive.

(b) *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.

(c) *Resident foreign corporations.* (1) 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).

(2) 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.

(3) 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, being a resident foreign corporation, is taxable upon all income derived from sources