







In addition, the President shall not designate any country a beneficiary country under this chapter -

(1) if such country is a Communist country;

(2) if such country -

(A) has nationalized, expropriated or otherwise seized ownership or control of property owned by a United States citizen or by a corporation, partnership, or association which is 50 per centum or more beneficially owned by United States citizens,

(B) has taken steps to repudiate or nullify -

(i) any existing contract or agreement with, or

(ii) any patent, trademark, or other intellectual property of a United States citizen or a corporation, partnership, or association which is 50 per centum or more beneficially owned by United States citizens, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of property so owned, or

(C) has imposed or enforced taxes or other exactions, restrictive maintenance or operational conditions, or other measures with respect to property so owned, the effect of which is to nationalize, expropriate, or otherwise seize ownership or control of such property, unless the President determines that -

- ⚭ (i) prompt, adequate, and effective compensation has been or is being made to such citizen, corporation, partnership, or association,
- ⚭ (ii) good-faith negotiations to provide prompt, adequate, and effective compensation under the applicable provisions of international law are in progress, or such country is otherwise taking steps to discharge its obligations under international law with respect to such citizen, corporation, partnership, or association, or
- ⚭ (iii) a dispute involving such citizen, corporation, partnership, or association, over compensation for such a seizure has been submitted to arbitration under the provisions of the Convention for the Settlement of Investment Disputes, or in another mutually agreed upon forum, and promptly furnishes a copy of such determination to the Senate and House of Representatives;

(3) if such country fails to act in good faith in recognizing as binding or in enforcing arbitral awards in favor of United States citizens or a corporation, partnership or association which is 50 per centum or more beneficially owned by United States citizens, which have been made by arbitrators appointed for each case or by permanent arbitral bodies to which the parties involved have submitted their dispute;

(4) if such country affords preferential treatment to the products of a developed country, other than the United States, which has, or is likely to have, a significant adverse effect on United States commerce, unless the President has received assurances satisfactory to him that such preferential treatment will be eliminated or that action will be taken to assure that there will be no such significant adverse effect, and he reports those assurances to the Congress;

(5) if a government-owned entity in such country engages in the broadcast of copyrighted material, including films or television material, belonging to United States copyright owners without their express consent;

(6) unless such country is a signatory to a treaty, convention, protocol, or other agreement regarding the extradition of United States citizens; and

(7) if such country has not or is not taking steps to afford internationally recognized worker rights (as defined in section 2467(4) of this title) to workers in the country (including any designated zone in that country). Paragraphs (1),

(2), (3), (5), and (7) shall not prevent the designation of any country as a beneficiary country under this Act if the President determines that such designation will be in the national economic or security interest of the United States and reports such determination to the Congress with his reasons therefor.

(c) Factors determining designation In determining whether to designate any country a beneficiary country under this chapter, the President shall take into account -

- ⊗ (1) an expression by such country of its desire to be so designated;
- ⊗ (2) the economic conditions in such country, the living standards of its inhabitants, and any other economic factors which he deems appropriate;
- ⊗ (3) the extent to which such country has assured the United States it will provide equitable and reasonable access to the markets and basic commodity resources of such country;
- ⊗ (4) the degree to which such country follows the accepted rules of international trade provided for under the WTO Agreement and the multilateral trade agreements (as such terms are defined in paragraphs (9) and (4), respectively, of section 3501 of this title);
- ⊗ (5) the degree to which such country uses export subsidies or imposes export performance requirements or local content requirements which distort international trade;
- ⊗ (6) the degree to which the trade policies of such country as they relate to other beneficiary countries are contributing to the revitalization of the region;
- ⊗ (7) the degree to which such country is undertaking self-help measures to promote its own economic development;
- ⊗ (8) whether or not such country has taken or is taking steps to afford to workers in that country (including any designated zone in that country) internationally recognized worker rights. Footnote 1.
- ⊗ (9) the extent to which such country provides under its law adequate and effective means for foreign nationals to secure, exercise, and enforce exclusive rights in intellectual property, including patent, trademark, and copyright rights;
- ⊗ (10) the extent to which such country prohibits its nationals from engaging in the broadcast of copyrighted material, including films or television material, belonging to United States copyright owners without their express consent; and
- ⊗ (11) the extent to which such country is prepared to cooperate with the United States in the administration of the provisions of this chapter.

(d) Omitted

(e) Withdrawal or suspension of duty-free treatment to specific articles

(1) The President may, after the requirements of subsection (a)(2) of this section and paragraph (2) have been met -

(A) withdraw or suspend the designation of any country as a beneficiary country, or

(B) withdraw, suspend, or limit the application of duty-free treatment under this chapter to any article of any country, if, after such designation, the President determines that as a result of changed circumstances such country would be barred from designation as a beneficiary country under subsection (b) of this section.

(2)

(A) The President shall publish in the Federal Register notice of the action the President proposes to take under paragraph (1) at least 30 days prior to taking such action.

(B) The United States Trade Representative shall, within the 30- day period beginning on the date on which the

President publishes under subparagraph (A) notice of proposed action -

(i) accept written comments from the public regarding such proposed action,

(ii) hold a public hearing on such proposed action, and

(iii) publish in the Federal Register -

- ⊗ (I) notice of the time and place of such hearing prior to the hearing, and
- ⊗ (II) the time and place at which such written comments will be accepted.

(f) Reporting requirements On or before October 1, 1993, and the close of each 3-year period thereafter, the President shall submit to the Congress a complete report regarding the operation of this chapter, including the results of a general review of beneficiary countries based on the considerations described in subsections (b) and (c) of this section.

Footnotes

[1] So in original. The period probably should be a semicolon.

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### **Sec. 2703.** Eligible articles

(a) Growth, product, or manufacture of beneficiary countries

(1) Unless otherwise excluded from eligibility by this chapter, and subject to section 423 of the Tax Reform Act of 1986, the duty-free treatment provided under this chapter shall apply to any article which is the growth, product, or manufacture of a beneficiary country if -

(A) that article is imported directly from a beneficiary country into the customs territory of the United States; and

(B) the sum of (i) the cost or value of the materials produced in a beneficiary country or two or more beneficiary countries, plus (ii) the direct costs of processing operations performed in a beneficiary country or countries is not less than 35 per centum of the appraised value of such article at the time it is entered. For purposes of determining the percentage referred to in subparagraph (B), the term "beneficiary country" includes the Commonwealth of Puerto Rico and the United States Virgin Islands. If the cost or value of materials produced in the customs territory of the United States (other than the Commonwealth of Puerto Rico) is included with respect to an article to which this paragraph applies, an amount not to exceed 15 per centum of the appraised value of the article at the time it is entered that is attributed to such United States cost or value may be applied toward determining the percentage referred to in subparagraph (B).

(2) The Secretary of the Treasury shall prescribe such regulations as may be necessary to carry out this subsection including, but not limited to, regulations providing that, in order to be eligible for duty-free treatment under this chapter, an article must be wholly the growth, product, or manufacture of a beneficiary country, or must be a new or different article of commerce which has been grown, produced, or manufactured in the beneficiary country; but no article or material of a beneficiary country shall be eligible for such treatment by virtue of having merely undergone -

(A) simple combining or packaging operations, or

(B) mere dilution with water or mere dilution with another substance that does not materially alter the characteristics of the article.

(3) As used in this subsection, the phrase "direct costs of processing operations" includes, but is not limited to -

(A) all actual labor costs involved in the growth, production, manufacture, or assembly of the specific merchandise, including fringe benefits, on-the-job training and the cost of engineering, supervisory, quality control, and similar personnel; and

(B) dies, molds, tooling, and depreciation on machinery and equipment which are allocable to the specific merchandise. Such phrase does not include costs which are not directly attributable to the merchandise concerned or are not costs of manufacturing the product, such as (i) profit, and (ii) general expenses of doing business which are either not allocable to the specific merchandise or are not related to the growth, production, manufacture, or assembly of the merchandise, such as administrative salaries, casualty and liability insurance, advertising, and salesmen's salaries, commissions or expenses.

(4) Notwithstanding section 1311 of this title, the products of a beneficiary country which are imported directly from any beneficiary country into Puerto Rico may be entered under bond for processing or use in manufacturing in Puerto Rico. No duty shall be imposed on the withdrawal from warehouse of the product of such processing or manufacturing if, at the time of such withdrawal, such product meets the requirements of paragraph (1)(B).

(5) The duty-free treatment provided under this chapter shall apply to an article (other than an article listed in subsection (b) of this section) which is the growth, product, or manufacture of the Commonwealth of Puerto Rico if -

(A) the article is imported directly from the beneficiary country into the customs territory of the United States,

(B) the article was by any means advanced in value or improved in condition in a beneficiary country, and

(C) if any materials are added to the article in a beneficiary country, such materials are a product of a beneficiary country or the United States.

(b) Articles to which duty-free treatment does not apply

The duty-free treatment provided under this chapter shall not apply to -

(1) textile and apparel articles which are subject to textile agreements;

(2) footwear not designated at the time of the effective date of this chapter (Aug. 5, 1983) as eligible articles for the purpose of the generalized system of preferences under title V of the Trade Act of 1974 (19 U.S.C. 2461 et seq.);

(3) tuna, prepared or preserved in any manner, in airtight containers;

(4) petroleum, or any product derived from petroleum, provided for in headings 2709 and 2710 of the Harmonized Tariff Schedule of the United States;

(5) watches and watch parts (including cases, bracelets and straps), of whatever type including, but not limited to, mechanical, quartz digital or quartz analog, if such watches or watch parts contain any material which is the product of any country with respect to which HTS column 2 rates of duty apply; or

(6) articles to which reduced rates of duty apply under subsection (h) of this section.

(c) Sugar and beef products; stable food production plan; suspension of duty-free treatment; monitoring

(1) As used in this subsection -

(A) The term "sugar and beef products" means -

(i) sugars, sirups, and molasses provided for in subheadings 1701.11.00, 1701.12.00, 1701.91.20, 1701.99.00, 1702.90.30, 1806.10.40, and 2106.90.10 of the Harmonized Tariff Schedule of the United States, and

(ii) articles of beef or veal, however provided for in chapters 2 and 16 of the Harmonized Tariff Schedule of the United States.

(B) The term "Plan" means a stable food production plan that consists of measures and proposals designed to ensure that the present level of food production in, and the nutritional level of the population of, a beneficiary country will not be adversely affected by changes in land use and land ownership that will result if increased production of sugar and beef products is undertaken in response to the duty-free treatment extended under this chapter to such products. A Plan must specify such facts regarding, and such proposed actions by, a beneficiary country as the President deems necessary for purposes of carrying out this subsection, including but not limited to -

(i) the current levels of food production and nutritional health of the population;

(ii) current level of production and export of sugar and beef products;

(iii) expected increases in production and export of sugar and beef products as a result of the duty-free access to the United States market provided under this chapter;

(iv) measures to be taken to ensure that the expanded production of those products because of such duty-free access will not occur at the expense of stable food production; and

(v) proposals for a system to monitor the impact of such duty-free access on stable food production and land use and land ownership patterns.

(2) Duty-free treatment extended under this chapter to sugar and beef products that are the product of a beneficiary country shall be suspended by the President under this subsection if -

(A) the beneficiary country, within the ninety-day period beginning on the date of its designation as such a country under section 2702 of this title, does not submit a Plan to the President for evaluation;

(B) on the basis of his evaluation, the President determines that the Plan of a beneficiary country does not meet the criteria set forth in paragraph (1)(B); or

(C) as a result of the monitoring of the operation of the Plan under paragraph (5), the President determines that a beneficiary country is not making a good faith effort to implement its Plan, or that the measures and proposals in the Plan, although being implemented, are not achieving their purposes.

(3) Before the President suspends duty-free treatment by reason of paragraph (2)(A), (B), or (C) to the sugar and beef products of a beneficiary country, he must offer to enter into consultation with the beneficiary country for purposes of formulating appropriate remedial action which may be taken by that country to avoid such suspension. If the beneficiary country thereafter enters into consultation within a reasonable time and undertakes to formulate remedial action in good faith, the President shall withhold the suspension of duty-free treatment on the condition that the

remedial action agreed upon be appropriately implemented by that country.

(4) The President shall monitor on a biennial basis the operation of the Plans implemented by beneficiary countries, and shall submit a written report to Congress by March 15 following the close of each biennium, that -

(A) specifies the extent to which each Plan, and remedial actions, if any, agreed upon under paragraph (4), have been implemented; and

(B) evaluates the results of such implementation.

(5) The President shall terminate any suspension of duty-free treatment imposed under this subsection if he determines that the beneficiary country has taken appropriate action to remedy the factors on which the suspension was based.

(d) Tariff-rate quotas

No quantity of an agricultural product subject to a tariff-rate quota that exceeds the in-quota quantity shall be eligible for duty-free treatment under this chapter.

(e) Proclamations suspending duty-free treatment

(1) The President may by proclamation suspend the duty-free treatment provided by this chapter with respect to any eligible article and may proclaim a duty rate for such article if such action is provided under chapter 1 of title II of the Trade Act of 1974 (19 U.S.C. 2251 et seq.) or section 1862 of this title.

(2) In any report by the International Trade Commission to the President under section 202(f) of the Trade Act of 1974 (19 U.S.C. 2252(f)) regarding any article for which duty-free treatment has been proclaimed by the President pursuant to this chapter, the Commission shall state whether and to what extent its findings and recommendations apply to such article when imported from beneficiary countries.

(3) For purposes of subsections [1] section 203 of the Trade Act of 1974 (19 U.S.C. 2253(a), (c)), the suspension of the duty-free treatment provided by this chapter shall be treated as an increase in duty. [1] So in original.

(4) No proclamation which provides solely for a suspension referred to in paragraph (3) of this subsection with respect to any article shall be taken under section 203 of the Trade Act of 1974 (19 U.S.C. 2253) unless the United States International Trade Commission, in addition to making an affirmative determination with respect to such article under section 202(b) of the Trade Act of 1974 (19 U.S.C. 2252(b)), determines in the course of its investigation under such section that the serious injury (or threat thereof) substantially caused by imports to the domestic industry producing a like or directly competitive article results from the duty-free treatment provided by this chapter.

(5)

(A) Any action taken under section 203 of the Trade Act of 1974 (19 U.S.C. 2253) that is in effect when duty-free treatment pursuant to section 2701 [2] of this title is proclaimed shall remain in effect until modified or terminated.

(B) If any article is subject to any such action at the time duty-free treatment is proclaimed pursuant to section 2701 of this title, the President may reduce or terminate the application of such action to the importation of such article from beneficiary countries prior to the otherwise scheduled date on which such reduction or termination would occur pursuant to the criteria and procedures of section 203 of the Trade Act of 1974 (19 U.S.C. 2253).

(f) Petitions to International Trade Commission

(1) If a petition is filed with the International Trade Commission pursuant to the provisions of section 201 of the Trade Act of 1974 (19 U.S.C. 2251) regarding a perishable product and alleging injury from imports from beneficiary countries, then the petition may also be filed with the Secretary of Agriculture with a request that emergency relief be granted pursuant to paragraph (3) of this subsection with respect to such article.

(2) Within fourteen days after the filing of a petition under paragraph (1) of this subsection -

(A) if the Secretary of Agriculture has reason to believe that a perishable product from a beneficiary country is being imported into the United States in such increased quantities as to be a substantial cause of serious injury, or the threat thereof, to the domestic industry producing a perishable product like or directly competitive with the imported product and that emergency action is warranted, he shall advise the President and recommend that the President take emergency action; or

(B) the Secretary of Agriculture shall publish a notice of his determination not to recommend the imposition of emergency action and so advise the petitioner.

(3) Within seven days after the President receives a recommendation from the Secretary of Agriculture to take emergency action pursuant to paragraph (2) of this subsection, he shall issue a proclamation withdrawing the duty-free treatment provided by this chapter or publish a notice of his determination not to take emergency action.

(4) The emergency action provided by paragraph (3) of this subsection shall cease to apply -

(A) upon the taking of action under section 203 of the Trade Act of 1974 (19 U.S.C. 2253),

(B) on the day a determination by the President not to take action [1] under section 203 of such Act (19 U.S.C. 2253) not to take action [1] becomes final,

(C) in the event of a report of the United States International Trade Commission containing a negative finding, on the day the Commission's report is submitted to the President, or

(D) whenever the President determines that because of changed circumstances such relief is no longer warranted.

(5) For purposes of this subsection, the term "perishable product" means -

(A) live plants and fresh cut flowers provided for in chapter 6 of the HTS;

(B) fresh or chilled vegetables provided for in headings 0701 through 0709 (except subheading 0709.52.00) and heading 0714 of the HTS;

(C) fresh fruit provided for in subheadings 0804.20 through 0810.90 (except citrons of subheading 0805.90.00, tamarinds and kiwi fruit of subheading 0810.90.20, and cashew apples, mameyes colorados, sapodillas, soursops and sweetsops of subheading 0810.90.40) of the HTS; and

(D) concentrated citrus fruit juice provided for in subheadings 2009.11.00, 2009.19.40, 2009.20.40, 2009.30.20, and 2009.30.60 of the HTS.

(g) Fees not affected by proclamation

No proclamation issued pursuant to this chapter shall affect fees imposed pursuant to section 624 of title 7.

(h) Duty reduction for certain leather-related products

(1) Subject to paragraph (2), the President shall proclaim reductions in the rates of duty on handbags, luggage, flat goods, work gloves, and leather wearing apparel that -

(A) are the product of any beneficiary country; and

(B) were not designated on August 5, 1983, as eligible articles for purposes of the generalized system of preferences under title V of the Trade Act of 1974 (19 U.S.C. 2461 et seq.).

(2) The reduction required under paragraph (1) in the rate of duty on any article shall -

(A) result in a rate that is equal to 80 percent of the rate of duty that applies to the article on December 31, 1991, except that, subject to the limitations in paragraph (3), the reduction may not exceed 2.5 percent ad valorem; and

(B) be implemented in 5 equal annual stages with the first one-fifth of the aggregate reduction in the rate of duty being applied to entries, or withdrawals from warehouse for consumption, of the article on or after January 1, 1992.

(3) The reduction required under this subsection with respect to the rate of duty on any article is in addition to any reduction in the rate of duty on that article that may be proclaimed by the President as being required or appropriate to carry out any trade agreement entered into under the Uruguay Round of trade negotiations; except that if the reduction so proclaimed -

(A) is less than 1.5 percent ad valorem, the aggregate of such proclaimed reduction and the reduction under this subsection may not exceed 3.5 percent ad valorem, or

(B) is 1.5 percent ad valorem or greater, the aggregate of such proclaimed reduction and the reduction under this subsection may not exceed the proclaimed reduction plus 1 percent ad valorem.

Footnotes

[2] See References in Text note below.

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**Sec. 2704.** International Trade Commission reports on impact of Caribbean Basin Economic Recovery Program

(a) Reporting requirement

The United States International Trade Commission (hereinafter in this section referred to as the "Commission") shall prepare, and submit to the Congress and to the President, a report regarding the economic impact of this Act on United States industries and consumers during -

(1) the twenty-four-month period beginning with August 5, 1983; and

(2) each calendar year occurring thereafter until duty-free treatment under this chapter is terminated under section 2706(b) [1] of this title.

(b) Requisite areas of Commission assessment

(1) Each report required under subsection (a) of this section shall include, but not be limited to, an assessment by the Commission regarding -

(A) the actual effect, during the period covered by the report, of this Act on the United States economy generally as well as on those specific domestic industries which produce articles that are like, or directly competitive with, articles being imported into the United States from beneficiary countries; and

(B) the probable future effect which this Act will have on the United States economy generally, as well as on such domestic industries, before the provisions of this Act terminate.

(2) In preparing the assessments required under paragraph (1), the Commission shall, to the extent practicable -

(A) analyze the production, trade and consumption of United States products affected by this Act, taking into consideration employment, profit levels, and use of productive facilities with respect to the domestic industries concerned, and such other economic factors in such industries as it considers relevant, including prices, wages, sales, inventories, patterns of demand, capital investment, obsolescence of equipment, and diversification of production; and

(B) describe the nature and extent of any significant change in employment, profit levels, and use of productive facilities, and such other conditions as it deems relevant in the domestic industries concerned, which it believes are attributable to this Act.

(c) Time of submission of reports; public participation

(1) Each report required under subsection (a) of this section shall be submitted to the Congress and to the President before the close of the nine-month period beginning on the day after the last day of the period covered by the report.

(2) The Commission shall provide opportunity for the submission by the public, either orally or in writing, or both, of information relating to matters that will be addressed in the reports.

Footnotes

[1] See References in Text note below. For purposes of this section, industries in the Commonwealth of Puerto Rico and the insular possessions of the United States shall be considered to be United States industries.

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**Sec. 2705.** Impact study by Secretary of Labor

The Secretary of Labor, in consultation [1] with other appropriate Federal agencies, shall undertake a continuing review and analysis of the impact which the implementation of the provisions of this chapter have with respect to United States labor; and shall make an annual written report to Congress on the results of such review and analysis.

Footnotes

[1] So in original. Probably should be "consultation".

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**Sec. 2706.** Effective date

- (a) This chapter shall take effect on August 5, 1983.
- (b) Repealed. Pub. L. 101-382, title II, Sec. 211, Aug. 20, 1990, 104 Stat. 655.

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**Sec. 936.** Puerto Rico and possession tax credit

- ⚭ (a) Allowance of credit
- ⚭ (1) In general Except as otherwise provided in this section, if a domestic corporation elects the application of this section and if the conditions of both subparagraph (A) and subparagraph (B) of paragraph (2) are satisfied, there shall be allowed as a credit against the tax imposed by this chapter an amount equal to the portion of the tax which is attributable to the sum of -
  - ⚭ (A) the taxable income, from sources without the United States, from -
    - ⚭ (i) the active conduct of a trade or business within a possession of the United States, or
    - ⚭ (ii) the sale or exchange of substantially all of the assets used by the taxpayer in the active conduct of such trade or business, and (B) the qualified possession source investment income.
  - ⚭ (2) Conditions which must be satisfied The conditions referred to in paragraph (1) are:
    - ⚭ (A) 3-year period If 80 percent or more of the gross income of such domestic corporation for the 3-year period immediately preceding the close of the taxable year (or for such part of such period immediately preceding the close of such taxable year as may be applicable) was derived from sources within a possession of the United States (determined without regard to section 904 (f)); and (B) Trade or business If 75 percent or more of the gross income of such domestic corporation for such period or such part thereof was derived from the active conduct of a trade or business within a possession of the United States.
  - ⚭ (3) Credit not allowed against certain taxes The credit provided by paragraph (1) shall not be allowed against the tax imposed by -
    - ⚭ (A) section 59A (relating to environmental tax),
    - ⚭ (B) section 531 (relating to the tax on accumulated earnings),
    - ⚭ (C) section 541 (relating to personal holding company tax), or
    - ⚭ (D) section 1351 (relating to recoveries of foreign expropriation losses).
  - ⚭ (4) Limitations on credit for active business income
    - ⚭ (A) In general The amount of the credit determined under paragraph (1) for any taxable year with respect to income referred to in subparagraph (A) thereof shall not exceed the sum of the following amounts:
      - ⚭ (i) 60 percent of the sum of -
        - ⚭ (I) the aggregate amount of the possession corporation's qualified possession wages for such taxable year, plus
        - ⚭ (II) the allocable employee fringe benefit expenses of the possession corporation for the taxable year.
      - ⚭ (ii) The sum of -
        - ⚭ (I) 15 percent of the depreciation allowances for the taxable year with respect to short-life qualified tangible property,
        - ⚭ (II) 40 percent of the depreciation allowances for the taxable year with respect to medium-life qualified tangible property, and (III) 65 percent of the depreciation allowances for the taxable year with respect to long-life qualified tangible property.
      - ⚭ (iii) If the possession corporation does not have an election to use the method described in subsection (h)(5)(C) (ii) (relating to profit split) in effect for the taxable year, the amount of qualified possession income taxes for the taxable year allocable to nonsheltered income.
    - ⚭ (B) Election to take reduced credit
      - ⚭ (i) In general If an election under this subparagraph applies to a possession corporation for any taxable year -

- ⊗ (I) subparagraph (A), and the provisions of subsection (i), shall not apply to such possession corporation for such taxable year, and (II) the credit determined under paragraph (1) for such taxable year with respect to income referred to in subparagraph (A) thereof shall be the applicable percentage of the credit which would otherwise have been determined under such paragraph with respect to such income. Notwithstanding subclause (I), a possession corporation to which an election under this subparagraph applies shall be entitled to the benefits of subsection (i)(3)(B) for taxes allocable (on a pro rata basis) to taxable income the tax on which is not offset by reason of this subparagraph.
- ⊗ (ii) Applicable percentage The term "applicable percentage" means the percentage determined in accordance with the following table: In the case of taxable The years beginning in: percentage is: 1994 60 1995 55 1996 50 1997 45 1998 and thereafter 40.
- ⊗ (iii) Election
- ⊗ (I) In general An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1993, for which it is a possession corporation.
- ⊗ (II) Period of election An election under this subparagraph shall apply to the taxable year for which made and all subsequent taxable years unless revoked.
- ⊗ (III) Affiliated groups If, for any taxable year, an election is not in effect for any possession corporation which is a member of an affiliated group, any election under this subparagraph for any other member of such group is revoked for such taxable year and all subsequent taxable years. For purposes of this subclause, members of an affiliated group shall be determined without regard to the exceptions contained in section 1504 (b) and as if the constructive ownership rules of section 1563(e) applied for purposes of section 1504(a). The Secretary may prescribe regulations to prevent the avoidance of this subclause through deconsolidation or otherwise.
- ⊗ (C) Cross reference For definitions and special rules applicable to this paragraph, see subsection (i).
- ⊗ (b) Amounts received in United States. In determining taxable income for purposes of subsection (a), there shall not be taken into account as income from sources without the United States any gross income which was received by such domestic corporation within the United States, whether derived from sources within or without the United States. This subsection shall not apply to any amount described in subsection (a)(1)(A)(i) received from a person who is not a related person (within the meaning of subsection (h)(3) but without regard to subparagraphs (D)(ii) and (E)(i) thereof) with respect to the domestic corporation.
- ⊗ (c) Treatment of certain foreign taxes. For purposes of this title, any tax of a foreign country or a possession of the United States which is paid or accrued with respect to taxable income which is taken into account in computing the credit under subsection (a) shall not be treated as income, war profits, or excess profits taxes paid or accrued to a foreign country or possession of the United States, and no deduction shall be allowed under this title with respect to any amounts so paid or accrued.
- ⊗ (d) Definitions and special rules. For purposes of this section -
- ⊗ (1) Possession The term "possession of the United States" includes the Commonwealth of Puerto Rico and the Virgin Islands.
- ⊗ (2) Qualified possession source investment income The term "qualified possession source investment income" means gross income which -
- ⊗ (A) is from sources within a possession of the United States in which a trade or business is actively conducted, and (B) the taxpayer establishes to the satisfaction of the Secretary is attributable to the investment in such possession (for use therein) of funds derived from the active conduct of a trade or business in such possession, or from such investment, less the deductions properly apportioned or allocated thereto.
- ⊗ (3) Carryover basis property
- ⊗ (A) In general Income from the sale or exchange of any asset the basis of which is determined in whole or in part by reference to its basis in the hands of another person shall not be treated as income described in subparagraph (A) or (B) of subsection (a)(1).
- ⊗ (B) Exception for possessions corporations, etc. For purposes of subparagraph (A), the holding of any asset by another person shall not be taken into account if throughout the period for which such asset was held by such person section 931, this section, or section 957(c) (as in effect on the day before the date of the enactment of the Tax Reform Act of 1986) applied to such person.
- ⊗ (4) Investment in qualified Caribbean Basin countries

- ⊗ (A) In general For purposes of paragraph (2)(B), an investment in a financial institution shall, subject to such conditions as the Secretary may prescribe by regulations, be treated as for use in Puerto Rico to the extent used by such financial institution (or by the Government Development Bank for Puerto Rico or the Puerto Rico Economic Development Bank) -
- ⊗ (i) for investment, consistent with the goals and purposes of the Caribbean Basin Economic Recovery Act, in -
- ⊗ (I) active business assets in a qualified Caribbean Basin country, or
- ⊗ (II) development projects in a qualified Caribbean Basin country, and (ii) in accordance with a specific authorization granted by the Commissioner of Financial Institutions of Puerto Rico pursuant to regulations issued by such Commissioner. A similar rule shall apply in the case of a direct investment in the Government Development Bank for Puerto Rico or the Puerto Rico Economic Development Bank.
- ⊗ (B) Qualified Caribbean Basin country For purposes of this subsection, the term "qualified Caribbean Basin country" means any beneficiary country (within the meaning of section 212(a)(1)(A) of the Caribbean Basin Economic Recovery Act) which meets the requirements of clauses
- ⊗ (i) and (ii) of section 274(h)(6)(A) and the Virgin Islands.
- ⊗ (C) Additional requirements Subparagraph (A) shall not apply to any investment made by a financial institution (or by the Government Development Bank for Puerto Rico or the Puerto Rico Economic Development Bank) unless -
- ⊗ (i) the person in whose trade or business such investment is made (or such other recipient of the investment) and the financial institution or such Bank certify to the Secretary and the Commissioner of Financial Institutions of Puerto Rico that the proceeds of the loan will be promptly used to acquire active business assets or to make other authorized expenditures, and (ii) the financial institution (or the Government Development Bank for Puerto Rico or the Puerto Rico Economic Development Bank) and the recipient of the investment funds agree to permit the Secretary and the Commissioner of Financial Institutions of Puerto Rico to examine such of their books and records as may be necessary to ensure that the requirements of this paragraph are met.
- ⊗ (D) Requirement for investment in Caribbean Basin countries
- ⊗ (i) In general For each calendar year, the government of Puerto Rico shall take such steps as may be necessary to ensure that at least \$100,000,000 of qualified Caribbean Basin country investments are made during such calendar year.
- ⊗ (ii) Qualified Caribbean Basin country investment For purposes of clause (i), the term "qualified Caribbean Basin country investment" means any investment if -
- ⊗ (I) the income from such investment is treated as qualified possession source investment income by reason of subparagraph (A), and (II) such investment is not (directly or indirectly) a refinancing of a prior investment (whether or not such prior investment was a qualified Caribbean Basin country investment).
- ⊗ (e) Election
- ⊗ (1) Period of election The election provided in subsection (a) shall be made at such time and in such manner as the Secretary may by regulations prescribe. Any such election shall apply to the first taxable year for which such election was made and for which the domestic corporation satisfied the conditions of subparagraphs (A) and (B) of subsection (a)(2) and for each taxable year thereafter until such election is revoked by the domestic corporation under paragraph (2). If any such election is revoked by the domestic corporation under paragraph (2), such domestic corporation may make a subsequent election under subsection (a) for any taxable year thereafter for which such domestic corporation satisfies the conditions of subparagraphs (A) and (B) of subsection (a)(2) and any such subsequent election shall remain in effect until revoked by such domestic corporation under paragraph (2).
- ⊗ (2) Revocation An election under subsection (a) -
- ⊗ (A) may be revoked for any taxable year beginning before the expiration of the 9th taxable year following the taxable year for which such election first applies only with the consent of the Secretary; and (B) may be revoked for any taxable year beginning after the expiration of such 9th taxable year without the consent of the Secretary.
- ⊗ (f) Limitation on credit for DISC's and FSC's. No credit shall be allowed under this section to a corporation for any taxable year -
- ⊗ (1) for which it is a DISC or former DISC, or

- ⊗ (2) in which it owns at any time stock in a -
- ⊗ (A) DISC or former DISC, or
- ⊗ (B) FSC or former FSC.
- ⊗ (g) Exception to accumulated earnings tax.
- ⊗ (1) For purposes of section 535, the term "accumulated taxable income" shall not include taxable income entitled to the credit under subsection (a).
- ⊗ (2) For purposes of section 537, the term "reasonable needs of the business" includes assets which produce income eligible for the credit under subsection (a).

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- ⊗ (h) Tax treatment of intangible property income.
- ⊗ (1) In general.
- ⊗ (A) Income attributable to shareholders The intangible property income of a corporation electing the application of this section for any taxable year shall be included on a pro rata basis in the gross income of all shareholders of such electing corporation at the close of the taxable year of such electing corporation as income from sources within the United States for the taxable year of such shareholder in which or with which the taxable year of such electing corporation ends.
- ⊗ (B) Exclusion from the income of an electing corporation Any intangible property income of a corporation electing the application of this section which is included in the gross income of a shareholder of such corporation by reason of subparagraph (A) shall be excluded from the gross income of such corporation.
- ⊗ (2) Foreign shareholders; shareholders not subject to tax.
- ⊗ (A) In general Paragraph (1)(A) shall not apply with respect to any shareholder -
- ⊗ (i) who is not a United States person, or
- ⊗ (ii) who is not subject to tax under this title on intangible property income which would be allocated to such shareholder (but for this subparagraph).
- ⊗ (B) Treatment of nonallocated intangible property income For purposes of this subtitle, intangible property income of a corporation electing the application of this section which is not included in the gross income of a shareholder of such corporation by reason of subparagraph (A) -
- ⊗ (i) shall be treated as income from sources within the United States, and (ii) shall not be taken into account under subsection (a)(2).
- ⊗ (3) Intangible property income. For purposes of this subsection -
- ⊗ (A) In general The term "intangible property income" means the gross income of a corporation attributable to any intangible property other than intangible property which has been licensed to such corporation since prior to 1948 and is in use by such corporation on the date of the enactment of this subparagraph.
- ⊗ (B) Intangible property The term "intangible property" means any -
- ⊗ (i) patent, invention, formula, process, design, pattern, or know-how;
- ⊗ (ii) copyright, literary, musical, or artistic composition;
- ⊗ (iii) trademark, trade name, or brand name;
- ⊗ (iv) franchise, license, or contract;
- ⊗ (v) method, program, system, procedure, campaign, survey, study, forecast, estimate, customer list, or technical data; or
- ⊗ (vi) any similar item, which has substantial value independent of the services of any individual.
- ⊗ (C) Exclusion of reasonable profit The term "intangible property income" shall not include any portion of the income from the sale, exchange or other disposition of any product, or from the rendering of services, by a corporation electing the application of this section which is determined by the Secretary to be a reasonable profit on the direct and indirect costs incurred by such electing corporation which are attributable to such income.
- ⊗ (D) Related person
- ⊗ (i) In general A person (hereinafter referred to as the "related person") is related to any person if -
- ⊗ (I) the related person bears a relationship to such person specified in section 267(b) or section 707(b)(1), or

- ⊗ (II) the related person and such person are members of the same controlled group of corporations.
- ⊗ (ii) Special rule For purposes of clause (i), section 267(b) and section 707(b)(1) shall be applied by substituting "10 percent" for "50 percent".
- ⊗ (E) Controlled group of corporations The term "controlled group of corporations" has the meaning given to such term by section 1563(a), except that -
- ⊗ (i) "more than 10 percent" shall be substituted for "at least 80 percent" and "more than 50 percent" each place either appears in section 563(a), and (ii) the determination shall be made without regard to subsections (a)(4), (b)(2), and (e)(3)(C) of section 1563.
- ⊗ (4) Distributions to meet qualification requirements.
- ⊗ (A) In general If the Secretary determines that a corporation does not satisfy a condition specified in subparagraph (A) or (B) of subsection (a)(2) for any taxable year by reason of the exclusion from gross income under paragraph (1)(B), such corporation shall nevertheless be treated as satisfying such condition for such year if it makes a pro rata distribution of property after the close of such taxable year to its shareholders (designated at the time of such distribution as a distribution to meet qualification requirements) with respect to their stock in an amount which is equal to -
- ⊗ (i) if the condition of subsection (a)(2)(A) is not satisfied, that portion of the gross income for the period described in subsection (a)(2)(A) -
- ⊗ (I) which was not derived from sources within a possession, and (II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the condition of subsection (a)(2)(A),
- ⊗ (ii) if the condition of subsection (a)(2)(B) is not satisfied, that portion of the gross income for such period -
- ⊗ (I) which was not derived from the active conduct of a trade or business within a possession, and (II) which exceeds the amount of such income for such period which would enable such corporation to satisfy the conditions of subsection (a)(2)(B), or
- ⊗ (iii) if neither of such conditions is satisfied, that portion of the gross income which exceeds the amount of gross income for such period which would enable such corporation to satisfy the conditions of subparagraphs (A) and (B) of subsection (a)(2).
- ⊗ (B) Effectively connected income In the case of a shareholder who is a nonresident alien individual or a foreign corporation, trust, or estate, any distribution described in subparagraph (A) shall be treated as income which is effectively connected with the conduct of a trade or business conducted through a permanent establishment of such shareholder within the United States.
- ⊗ (C) Distribution denied in case of fraud or willful neglect Subparagraph (A) shall not apply to a corporation if the determination of the Secretary described in subparagraph (A) contains a finding that the failure of such corporation to satisfy the conditions in subsection (a)(2) was due in whole or in part to fraud with intent to evade tax or willful neglect on the part of such corporation.
- ⊗ (5) Election out.
- ⊗ (A) In general The rules contained in paragraphs (1) through (4) do not apply for any taxable year if an election pursuant to subparagraph (F) is in effect to use one of the methods specified in subparagraph (C).
- ⊗ (B) Eligibility
- ⊗ (i) Requirement of significant business presence An election may be made to use one of the methods specified in subparagraph (C) with respect to a product or type of service only if an electing corporation has a significant business presence in a possession with respect to such product or type of service. An election may remain in effect with respect to such product or type of service for any subsequent taxable year only if such electing corporation maintains a significant business presence in a possession with respect to such product or type of service in such subsequent taxable year. If an election is not in effect for a taxable year because of the preceding sentence, the electing corporation shall be deemed to have revoked the election on the first day of such taxable year.
- ⊗ (ii) Definition For purposes of this subparagraph, an electing corporation has a "significant business presence" in a possession for a taxable year with respect to a product or type of service if:
- ⊗ (I) the total production costs (other than direct material costs and other than interest excluded by regulations prescribed by the Secretary) incurred by the electing corporation in the possession in producing units of that product sold or otherwise disposed of during the taxable year by the affiliated group to persons who are not

- members of the affiliated group are not less than 25 percent of the difference between (a) the gross receipts from sales or other dispositions during the taxable year by the affiliated group to persons who are not members of the affiliated group of such units of the product produced, in whole or in part, by the electing corporation in the possession, and (b) the direct material costs of the purchase of materials for such units of that product by all members of the affiliated group from persons who are not members of the affiliated group; or
- ⊗ (II) no less than 65 percent of the direct labor costs of the affiliated group for units of the product produced during the taxable year in whole or in part by the electing corporation or for the type of service rendered by the electing corporation during the taxable year, is incurred by the electing corporation and is compensation for services performed in the possession; or
  - ⊗ (III) with respect to purchases and sales by an electing corporation of all goods not produced in whole or in part by any member of the affiliated group and sold by the electing corporation to persons other than members of the affiliated group, no less than 65 percent of the total direct labor costs of the affiliated group in connection with all purchases and sales of such goods sold during the taxable year by such electing corporation is incurred by such electing corporation and is compensation for services performed in the possession. Notwithstanding satisfaction of one of the foregoing tests, an electing corporation shall not be treated as having a significant business presence in a possession with respect to a product produced in whole or in part by the electing corporation in the possession, for purposes of an election to use the method specified in subparagraph (C)(ii), unless such product is manufactured or produced in the possession by the electing corporation within the meaning of subsection (d)(1)(A) of section 954.
  - ⊗ (iii) Special rules
  - ⊗ (I) An electing corporation which produces a product or renders a type of service in a possession on the date of the enactment of this clause is not required to meet the significant business presence test in a possession with respect to such product or type of service for its taxable years beginning before January 1, 1986.
  - ⊗ (II) For purposes of this subparagraph, the costs incurred by an electing corporation or any other member of the affiliated group in connection with contract manufacturing by a person other than a member of the affiliated group, or in connection with a similar arrangement thereto, shall be treated as direct labor costs of the affiliated group and shall not be treated as production costs incurred by the electing corporation in the possession or as direct material costs or as compensation for services performed in the possession, except to the extent as may be otherwise provided in regulations prescribed by the Secretary.
  - ⊗ (iv) Regulations The Secretary may prescribe regulations setting forth:
    - ⊗ (I) an appropriate transitional (but not in excess of three taxable years) significant business presence test for commencement in a possession of operations with respect to products or types of service after the date of the enactment of this clause and not described in subparagraph (B)(iii)(I),
    - ⊗ (II) a significant business presence test for other appropriate cases, consistent with the tests specified in subparagraph (B)(ii),
    - ⊗ (III) rules for the definition of a product or type of service, and (IV) rules for treating components produced in whole or in part by a related person as materials, and the costs (including direct labor costs) related thereto as a cost of materials, where there is an independent resale price for such components or where otherwise consistent with the intent of the substantial business presence tests.
  - ⊗ (C) Methods of computation of taxable income If an election of one of the following methods is in effect pursuant to subparagraph (F) with respect to a product or type of service, an electing corporation shall compute its income derived from the active conduct of a trade or business in a possession with respect to such product or type of service in accordance with the method which is elected.
    - ⊗ (i) Cost sharing
    - ⊗ (I) Payment of cost sharing If an election of this method is in effect, the electing corporation must make a payment for its share of the cost (if any) of product area research which is paid or accrued by the affiliated group during that taxable year. Such share shall not be less than the same proportion of 110 percent of the cost of such product area research which the amount of "possession sales" bears to the amount of "total sales" of the affiliated group. The cost of product area research paid or accrued solely by the electing corporation in a taxable year (excluding amounts paid directly or indirectly to or on behalf of related persons and excluding amounts paid under any cost sharing agreements with related persons) will reduce (but not below zero) the

amount of the electing corporation's cost sharing payment under this method for that year. In the case of intangible property described in subsection (h)(3)(B)(i) which the electing corporation is treated as owning under subclause (II), in no event shall the payment required under this subclause be less than the inclusion or payment which would be required under section 367(d)(2)(A)(ii) or section 482 if the electing corporation were a foreign corporation.

- ⚡ (a) Product area research For purposes of this section, the term "product area research" includes (notwithstanding any provision to the contrary) the research, development and experimental costs, losses, expenses and other related deductions - including amounts paid or accrued for the performance of research or similar activities by another person; qualified research expenses within the meaning of section 41(b); amounts paid or accrued for the use of, or the right to use, research or any of the items specified in subsection (h)(3)(B)(i); and a proper allowance for amounts incurred for the acquisition of any of the items specified in subsection (h)(3)(B)(i) - which are properly apportioned or allocated to the same product area as that in which the electing corporation conducts its activities, and a ratable part of any such costs, losses, expenses and other deductions which cannot definitely be allocated to a particular product area.
- ⚡ (b) Affiliated group For purposes of this subsection, the term "affiliated group" shall mean the electing corporation and all other organizations, trades or businesses (whether or not incorporated, whether or not organized in the United States, and whether or not affiliated) owned or controlled directly or indirectly by the same interests, within the meaning of section 482.
- ⚡ (c) Possession sales For purposes of this section, the term "possession sales" means the aggregate sales or other dispositions for the taxable year to persons who are not members of the affiliated group by members of the affiliated group of products produced, in whole or in part, by the electing corporation in the possession which are in the same product area as is used for determining the amount of product area research, and of services rendered, in whole or in part, in the possession in such product area to persons who are not members of the affiliated group.
- ⚡ (d) Total sales For purposes of this section, the term "total sales" means the aggregate sales or other dispositions for the taxable year to persons who are not members of the affiliated group by members of the affiliated group of all products in the same product area as is used for determining the amount of product area research, and of services rendered in such product area to persons who are not members of the affiliated group.
- ⚡ (e) Product area For purposes of this section, the term "product area" shall be defined by reference to the three-digit classification of the Standard Industrial Classification code. The Secretary may provide for the aggregation of two or more three-digit classifications where appropriate, and for a classification system other than the Standard Industrial Classification code in appropriate cases.
- ⚡ (II) Effect of election For purposes of determining the amount of its gross income derived from the active conduct of a trade or business in a possession with respect to a product produced by, or type of service rendered by, the electing corporation for a taxable year, if an election of this method is in effect, the electing corporation shall be treated as the owner (for purposes of obtaining a return thereon) of intangible property described in subsection (h)(3)(B)(i) which is related to the units of the product produced, or type of service rendered, by the electing corporation. Such electing corporation shall not be treated as the owner (for purposes of obtaining a return thereon) of any intangible property described in subsection (h)(3)(B)(ii) through (v) (to the extent not described in subsection (h)(3)(B)(i)) or of any other nonmanufacturing intangible. Notwithstanding the preceding sentence, an electing corporation shall be treated as the owner (for purposes of obtaining a return thereon) of (a) intangible property which was developed solely by such corporation in a possession and is owned by such corporation, (b) intangible property described in subsection (h)(3)(B)(i) acquired by such corporation from a person who was not related to such corporation (or to any person related to such corporation) at the time of, or in connection with, such acquisition, and (c) any intangible property described in subsection (h)(3)(B)(ii) through (v) (to the extent not described in subsection (h)(3)(B)(i)) and other nonmanufacturing intangibles which relate to sales of units of products, or services rendered, to unrelated persons for ultimate consumption or use in the possession in which the electing corporation conducts its trade or business.
- ⚡ (III) Payment provisions
- ⚡ (a) The cost sharing payment determined under subparagraph (C)(i)(I) for any taxable year shall be made to the

person or persons specified in subparagraph (C)(i)(IV)(a) not later than the time prescribed by law for filing the electing corporation's return for such taxable year (including any extensions thereof). If all or part of such payment is not timely made, the amount of the cost sharing payment required to be paid shall be increased by the amount of interest that would have been due under section 6601(a) had the portion of the cost sharing payment that is not timely made been an amount of tax imposed by this title and had the last date prescribed for payment been the due date of the electing corporations (Footnote 1) return (determined without regard to any extension thereof). The amount by which a cost sharing payment determined under subparagraph (C)(i)(I) is increased by reason of the preceding sentence shall not be treated as a cost sharing payment or as interest. If failure to make timely payment is due in whole or in part to fraud or willful neglect, the electing corporation shall be deemed to have revoked the election made under subparagraph (A) on the first day of the taxable year for which the cost sharing payment was required.

- ⌘ (b) For purposes of this title, any tax of a foreign country or possession of the United States which is paid or accrued with respect to the payment or receipt of a cost sharing payment determined under subparagraph (C)(i)(I) or of an amount of increase referred to in subparagraph (C)(i)(III)(a) shall not be treated as income, war profits, or excess profits taxes paid or accrued to a foreign country or possession of the United States, and no deduction shall be allowed under this title with respect to any amounts of such tax so paid or accrued.
- ⌘ (IV) Special rules
- ⌘ (a) The amount of the cost sharing payment determined under subparagraph (C)(i)(I), and any increase in the amount thereof in accordance with subparagraph (C)(i)(III)(a), shall not be treated as income of the recipient, but shall reduce the amount of the deductions (and the amount of reductions in earnings and profits) otherwise allowable to the appropriate domestic member or members (other than an electing corporation) of the affiliated group, or, if there is no such domestic member, to the foreign member or members of such affiliated group as the Secretary may provide under regulations.
- ⌘ (b) If an election of this method is in effect, the electing corporation shall determine its intercompany pricing under the appropriate section 482 method, provided, however, that an electing corporation shall not be denied use of the resale price method for purposes of such intercompany pricing merely because the reseller adds more than an insubstantial amount to the value of the product by the use of intangible property.
- ⌘ (c) The amount of qualified research expenses, within the meaning of section 41, of any member of the controlled group of corporations (as defined in section 41(f)) of which the electing corporation is a member shall not be affected by the cost sharing payment required under this method.
- ⌘ (ii) Profit split
- ⌘ (I) General rule If an election of this method is in effect, the electing corporation's taxable income derived from the active conduct of a trade or business in a possession with respect to units of a product produced or type of service rendered, in whole or in part, by the electing corporation shall be equal to 50 percent of the combined taxable income of the affiliated group (other than foreign affiliates) derived from covered sales of units of the product produced or type of service rendered, in whole or in part, by the electing corporation in a possession.
- ⌘ (II) Computation of combined taxable income Combined taxable income shall be computed separately for each product produced or type of service rendered, in whole or in part, by the electing corporation in a possession. Combined taxable income shall be computed (notwithstanding any provision to the contrary) for each such product or type of service rendered by deducting from the gross income of the affiliated group (other than foreign affiliates) derived from covered sales of such product or type of service all expenses, losses, and other deductions properly apportioned or allocated to gross income from such sales or services, and a ratable part of all expenses, losses, or other deductions which cannot definitely be allocated to some item or class of gross income, which are incurred by the affiliated group (other than foreign affiliates). Notwithstanding any other provision to the contrary, in computing the combined taxable income for each such product or type of service rendered, the research, development, and experimental costs, expenses and related deductions for the taxable year which would otherwise be apportioned or allocated to the gross income of the affiliated group (other than foreign affiliates) derived from covered sales of such product produced or type of service rendered, in whole or in part, by the electing corporation in a possession, shall not be less than the same proportion of the amount of the share of product area research determined under subparagraph (C)(i)(I) (without regard to the third and fourth sentences thereof, but substituting "120 percent" for "110 percent" in the second sentence thereof) in the

- product area which includes such product or type of service, that such gross income from the product or type of service bears to such gross income from all products and types of services, within such product area, produced or rendered, in whole or part, by the electing corporation in a possession.
- ⚭ (III) Division of combined taxable income 50 percent of the combined taxable income computed as provided in subparagraph (C)(ii)(II) shall be allocated to the electing corporation. Combined taxable income, computed without regard to the last sentence of subparagraph (C)(ii)(II), less the amount allocated to the electing corporation under the preceding sentence, shall be allocated to the appropriate domestic member or members (other than any electing corporation) of the affiliated group and shall be treated as income from sources within the United States, or, if there is no such domestic member, to a foreign member or members of such affiliated group as the Secretary may provide under regulations.
  - ⚭ (IV) Covered sales For purposes of this paragraph, the term "covered sales" means sales by members of the affiliated group (other than foreign affiliates) to persons who are not members of the affiliated group or to foreign affiliates.
  - ⚭ (D) Unrelated person For purposes of this paragraph, the term "unrelated person" means any person other than a person related within the meaning of paragraph (3)(D) to the electing corporation.
  - ⚭ (E) Electing corporation For purposes of this subsection, the term "electing corporation" means a domestic corporation for which an election under this section is in effect.
  - ⚭ (F) Time and manner of election; revocation
  - ⚭ (i) In general An election under subparagraph (A) to use one of the methods under subparagraph (C) shall be made only on or before the due date prescribed by law (including extensions) for filing the tax return of the electing corporation for its first taxable year beginning after December 31, 1982. If an election of one of such methods is made, such election shall be binding on the electing corporation and such method must be used for each taxable year thereafter until such election is revoked by the electing corporation under subparagraph (F) (iii). If any such election is revoked by the electing corporation under subparagraph (F)(iii), such electing corporation may make a subsequent election under subparagraph (A) only with the consent of the Secretary.
  - ⚭ (ii) Manner of making election An election under subparagraph (A) to use one of the methods under subparagraph (C) shall be made by filing a statement to such effect with the return referred to in subparagraph (F)(i) or in such other manner as the Secretary may prescribe by regulations.
  - ⚭ (iii) Revocation
  - ⚭ (I) Except as provided in subparagraph (F)(iii)(II), an election may be revoked for any taxable year only with the consent of the Secretary.
  - ⚭ (II) An election shall be deemed revoked for the year in which the electing corporation is deemed to have revoked such election under subparagraph (B)(i) or (C)(i)(III)(a).
  - ⚭ (iv) Aggregation
  - ⚭ (I) Where more than one electing corporation in the affiliated group produces any product or renders any services in the same product area, all such electing corporations must elect to compute their taxable income under the same method under subparagraph (C).
  - ⚭ (II) All electing corporations in the same affiliated group that produce any products or render any services in the same product area may elect, subject to such terms and conditions as the Secretary may prescribe by regulations, to compute their taxable income from export sales under a different method from that used for all other sales and services. For this purpose, export sales means all sales by the electing corporation of products to foreign persons for use or consumption outside the United States and its possessions, provided such products are manufactured or produced in the possession within the meaning of subsection (d)(1)(A) of section 954, and further provided (except to the extent otherwise provided by regulations) the income derived by such foreign person on resale of such products (in the same state or in an altered state) is not included in foreign base company income for purposes of section 954(a).
  - ⚭ (III) All members of an affiliated group must consent to an election under this subsection at such time and in such manner as shall be prescribed by the Secretary by regulations.
  - ⚭ (6) Treatment of certain sales made after July 1, 1982
  - ⚭ (A) In general For purposes of this section, in the case of a disposition of intangible property made by a corporation after July 1, 1982, any gain or loss from such disposition shall be treated as gain or loss from

sources within the United States to which paragraph (5) does not apply.

- ⊗ (B) Exception Subparagraph (A) shall not apply to any disposition by a corporation of intangible property if such disposition is to a person who is not a related person to such corporation.
- ⊗ (C) Paragraph does not affect eligibility This paragraph shall not apply for purposes of determining whether the corporation meets the requirements of subsection (a)(2).
- ⊗ (7) Section 864(e)(1) not to apply This subsection shall be applied as if section 864(e)(1) (relating to treatment of affiliated groups) had not been enacted.
- ⊗ (8) Regulations. The Secretary shall prescribe such regulations as may be necessary or appropriate to carry out the purposes of this subsection, including rules for the application of this subsection to income from leasing of products to unrelated persons.

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- ⊗ (i) Definitions and special rules relating to limitations of subsection (a)(4)
- ⊗ (1) Qualified possession wages. For purposes of this section -
- ⊗ (A) In general The term "qualified possession wages" means wages paid or incurred by the possession corporation during the taxable year in connection with the active conduct of a trade or business within a possession of the United States to any employee for services performed in such possession, but only if such services are performed while the principal place of employment of such employee is within such possession.
- ⊗ (B) Limitation on amount of wages taken into account
- ⊗ (i) In general The amount of wages which may be taken into account under subparagraph (A) with respect to any employee for any taxable year shall not exceed 85 percent of the contribution and benefit base determined under section 230 of the Social Security Act for the calendar year in which such taxable year begins.
- ⊗ (ii) Treatment of part-time employees, etc. If -
- ⊗ (I) any employee is not employed by the possession corporation on a substantially full-time basis at all times during the taxable year, or
- ⊗ (II) the principal place of employment of any employee with the possession corporation is not within a possession at all times during the taxable year, the limitation applicable under clause (i) with respect to such employee shall be the appropriate portion (as determined by the Secretary) of the limitation which would otherwise be in effect under clause (i).
- ⊗ (C) Treatment of certain employees The term "qualified possession wages" shall not include any wages paid to employees who are assigned by the employer to perform services for another person, unless the principal trade or business of the employer is to make employees available for temporary periods to other persons in return for compensation. All possession corporations treated as 1 corporation under paragraph (5) shall be treated as 1 employer for purposes of the preceding sentence.
- ⊗ (D) Wages
- ⊗ (i) In general Except as provided in clause (ii), the term "wages" has the meaning given to such term by subsection (b) of section 3306 (determined without regard to any dollar limitation contained in such section). For purposes of the preceding sentence, such subsection (b) shall be applied as if the term "United States" included all possessions of the United States.
- ⊗ (ii) Special rule for agricultural labor and railway labor In any case to which subparagraph (A) or (B) of paragraph (1) of section 51(h) applies, the term "wages" has the meaning given to such term by section 51(h) (2).
- ⊗ (2) Allocable employee fringe benefit expenses
- ⊗ (A) In general The allocable employee fringe benefit expenses of any possession corporation for any taxable year is an amount which bears the same ratio to the amount determined under subparagraph (B) for such taxable year as -
- ⊗ (i) the aggregate amount of the possession corporation's qualified possession wages for such taxable year, bears to
- ⊗ (ii) the aggregate amount of the wages paid or incurred by such possession corporation during such taxable year. In no event shall the amount determined under the preceding sentence exceed 15 percent of the amount

referred to in clause

- ≠ (iii) the aggregate amount of the wages paid or incurred by
- ≠ (B) Expenses taken into account For purposes of subparagraph (A), the amount determined under this subparagraph for any taxable year is the aggregate amount allowable as a deduction under this chapter to the possession corporation for such taxable year with respect to -
  - ≠ (i) employer contributions under a stock bonus, pension, profit-sharing, or annuity plan,
  - ≠ (ii) employer-provided coverage under any accident or health plan for employees, and (iii) the cost of life or disability insurance provided to employees. Any amount treated as wages under paragraph (1)(D) shall not be taken into account under this subparagraph.
- ≠ (3) Treatment of possession taxes.
- ≠ (A) Amount of credit for possession corporations not using profit split
  - ≠ (i) In general For purposes of subsection (a)(4)(A)(iii), the amount of the qualified possession income taxes for any taxable year allocable to nonsheltered income shall be an amount which bears the same ratio to the possession income taxes for such taxable year as -
    - ≠ (I) the increase in the tax liability of the possession corporation under this chapter for the taxable year by reason of subsection (a)(4)(A) (without regard to clause
    - ≠ (iii) thereof), bears to
    - ≠ (II) the tax liability of the possession corporation under this chapter for the taxable year determined without regard to the credit allowable under this section.
  - ≠ (ii) Limitation on amount of taxes taken into account Possession income taxes shall not be taken into account under clause (i) for any taxable year to the extent that the amount of such taxes exceeds 9 percent of the amount of the taxable income for such taxable year.
- ≠ (B) Deduction for possession corporations using profit split Notwithstanding subsection (c), if a possession corporation is not described in subsection (a)(4)(A)(iii) for the taxable year, such possession corporation shall be allowed a deduction for such taxable year in an amount which bears the same ratio to the possession income taxes for such taxable year as -
  - ≠ (i) the increase in the tax liability of the possession corporation under this chapter for the taxable year by reason of subsection (a)(4)(A), bears to
  - ≠ (ii) the tax liability of the possession corporation under this chapter for the taxable year determined without regard to the credit allowable under this section. In determining the credit under subsection (a) and in applying the preceding sentence, taxable income shall be determined without regard to the preceding sentence.
- ≠ (C) Possession income taxes For purposes of this paragraph, the term "possession income taxes" means any taxes of a possession of the United States which are treated as not being income, war profits, or excess profits taxes paid or accrued to a possession of the United States by reason of subsection (c).
- ≠ (4) Depreciation rules. For purposes of this section -
  - ≠ (A) Depreciation allowances The term "depreciation allowances" means the depreciation deductions allowable under section 167 to the possession corporation.
  - ≠ (B) Categories of property
    - ≠ (i) Qualified tangible property The term "qualified tangible property" means any tangible property used by the possession corporation in a possession of the United States in the active conduct of a trade or business within such possession.
    - ≠ (ii) Short-life qualified tangible property The term "short-life qualified tangible property" means any qualified tangible property to which section 168 applies and which is 3-year property or 5-year property for purposes of such section.
    - ≠ (iii) Medium-life qualified tangible property The term "medium-life qualified tangible property" means any qualified tangible property to which section 168 applies and which is 7-year property or 10-year property for purposes of such section.
    - ≠ (iv) Long-life qualified tangible property The term "long-life qualified tangible property" means any qualified tangible property to which section 168 applies and which is not described in clause (ii) or (iii).
    - ≠ (v) Transitional rule In the case of any qualified tangible property to which section 168 (as in effect on the day before the date of the enactment of the Tax Reform Act of 1986) applies, any reference in this paragraph to

section 168 shall be treated as a reference to such section as so in effect.

- ⚭ (5) Election to compute credit on consolidated basis
- ⚭ (A) In general Any affiliated group may elect to treat all possession corporations which would be members of such group but for section 1504(b)(3) or (4) as 1 corporation for purposes of this section. The credit determined under this section with respect to such 1 corporation shall be allocated among such possession corporations in such manner as the Secretary may prescribe.
- ⚭ (B) Election An election under subparagraph (A) shall apply to the taxable year for which made and all succeeding taxable years unless revoked with the consent of the Secretary.
- ⚭ (6) Possession corporation. The term "possession corporation" means a domestic corporation for which the election provided in subsection (a) is in effect.

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- ⚭ (j) Termination
- ⚭ (1) In general. Except as otherwise provided in this subsection, this section shall not apply to any taxable year beginning after December 31, 1995.
- ⚭ (2) Transition rules for active business income credit. Except as provided in paragraph (3)
- ⚭ (A) Economic activity credit In the case of an existing credit claimant -
- ⚭ (i) with respect to a possession other than Puerto Rico, and (ii) to which subsection (a)(4)(B) does not apply, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 2002.
- ⚭ (B) Special rule for reduced credit
- ⚭ (i) In general In the case of an existing credit claimant to which subsection (a)(4)(B) applies, the credit determined under subsection (a)(1)(A) shall be allowed for taxable years beginning after December 31, 1995, and before January 1, 1998.
- ⚭ (ii) Election irrevocable after 1997 An election under subsection (a)(4)(B)(iii) which is in effect for the taxpayer's last taxable year beginning before 1997 may not be revoked unless it is revoked for the taxpayer's first taxable year beginning in 1997 and all subsequent taxable years.
- ⚭ (C) Economic activity credit for Puerto Rico For economic activity credit for Puerto Rico, see section 30A.
- ⚭ (3) Additional restricted credit.
- ⚭ (A) In general In the case of an existing credit claimant -
- ⚭ (i) the credit under subsection (a)(1)(A) shall be allowed for the period beginning with the first taxable year after the last taxable year to which subparagraph (A) or (B) of paragraph (2), whichever is appropriate, applied and ending with the last taxable year beginning before January 1, 2006, except that
- ⚭ (ii) the aggregate amount of taxable income taken into account under subsection (a)(1)(A) for any such taxable year shall not exceed the adjusted base period income of such claimant.
- ⚭ (B) Coordination with subsection (a)(4) The amount of income described in subsection (a)(1)(A) which is taken into account in applying subsection (a)(4) shall be such income as reduced under this paragraph.
- ⚭ (4) Adjusted base period income. For purposes of paragraph (3) -
- ⚭ (A) In general The term "adjusted base period income" means the average of the inflation-adjusted possession incomes of the corporation for each base period year.
- ⚭ (B) Inflation-adjusted possession income For purposes of subparagraph (A), the inflation-adjusted possession income of any corporation for any base period year shall be an amount equal to the sum of -
- ⚭ (i) the possession income of such corporation for such base period year, plus
- ⚭ (ii) such possession income multiplied by the inflation adjustment percentage for such base period year.
- ⚭ (C) Inflation adjustment percentage For purposes of subparagraph (B), the inflation adjustment percentage for any base period year means the percentage (if any) by which -
- ⚭ (i) the CPI for 1995, exceeds
- ⚭ (ii) the CPI for the calendar year in which the base period year for which the determination is being made ends. For purposes of the preceding sentence, the CPI for any calendar year is the CPI (as defined in section 1(f)(5)) for such year under section 1(f)(4).

- ⊗ (D) Increase in inflation adjustment percentage for growth during base years The inflation adjustment percentage (determined under subparagraph (C) without regard to this subparagraph) for each of the 5 taxable years referred to in paragraph (5)(A) shall be increased by -
  - ⊗ (i) 5 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1995;
  - ⊗ (ii) 10.25 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1994;
  - ⊗ (iii) 15.76 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1993;
  - ⊗ (iv) 21.55 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1992; and (v) 27.63 percentage points in the case of a taxable year ending during the 1-year period ending on October 13, 1991.
- ⊗ (5) Base period year. For purposes of this subsection -
  - ⊗ (A) In general The term "base period year" means each of 3 taxable years which are among the 5 most recent taxable years of the corporation ending before October 14, 1995, determined by disregarding -
    - ⊗ (i) one taxable year for which the corporation had the largest inflation-adjusted possession income, and (ii) one taxable year for which the corporation had the smallest inflation-adjusted possession income.
  - ⊗ (B) Corporations not having significant possession income throughout 5-year period
    - ⊗ (i) In general If a corporation does not have significant possession income for each of the most recent 5 taxable years ending before October 14, 1995, then, in lieu of applying subparagraph (A), the term "base period year" means only those taxable years (of such 5 taxable years) for which the corporation has significant possession income; except that, if such corporation has significant possession income for 4 of such 5 taxable years, the rule of subparagraph (A)(ii) shall apply.
    - ⊗ (ii) Special rule If there is no year (of such 5 taxable years) for which a corporation has significant possession income -
      - ⊗ (I) the term "base period year" means the first taxable year ending on or after October 14, 1995, but
      - ⊗ (II) the amount of possession income for such year which is taken into account under paragraph (4) shall be the amount which would be determined if such year were a short taxable year ending on September 30, 1995.
      - ⊗ (iii) Significant possession income For purposes of this subparagraph, the term "significant possession income" means possession income which exceeds 2 percent of the possession income of the taxpayer for the taxable year (of the period of 6 taxable years ending with the first taxable year ending on or after October 14, 1995) having the greatest possession income.
  - ⊗ (C) Election to use one base period year
    - ⊗ (i) In general At the election of the taxpayer, the term "base period year" means -
      - ⊗ (I) only the last taxable year of the corporation ending in calendar year 1992, or
      - ⊗ (II) a deemed taxable year which includes the first ten months of calendar year 1995.
    - ⊗ (ii) Base period income for 1995 In determining the adjusted base period income of the corporation for the deemed taxable year under clause (i)(II), the possession income shall be annualized and shall be determined without regard to any extraordinary item.
    - ⊗ (iii) Election An election under this subparagraph by any possession corporation may be made only for the corporation's first taxable year beginning after December 31, 1995, for which it is a possession corporation. The rules of subclauses (II) and (III) of subsection (a)(4)(B)(iii) shall apply to the election under this subparagraph.
  - ⊗ (D) Acquisitions and dispositions Rules similar to the rules of subparagraphs (A) and (B) of section 41(f)(3) shall apply for purposes of this subsection.
- ⊗ (6) Possession income. For purposes of this subsection, the term "possession income" means, with respect to any possession, the income referred to in subsection (a)(1)(A) determined with respect to that possession. In no event shall possession income be treated as being less than zero.
- ⊗ (7) Short years. If the current year or a base period year is a short taxable year, the application of this subsection shall be made with such annualizations as the Secretary shall prescribe.
- ⊗ (8) Special rules for certain possessions.
- ⊗ (A) In general In the case of an existing credit claimant with respect to an applicable possession, this section

- (other than the preceding paragraphs of this subsection) shall apply to such claimant with respect to such applicable possession for taxable years beginning after December 31, 1995, and before January 1, 2006.
- ⚭ (B) Applicable possession For purposes of this paragraph, the term "applicable possession" means Guam, American Samoa, and the Commonwealth of the Northern Mariana Islands.
  - ⚭ (9) Existing credit claimant. For purposes of this subsection -
  - ⚭ (A) In general The term "existing credit claimant" means a corporation -
  - ⚭ (i)
  - ⚭ (I) which was actively conducting a trade or business in a possession on October 13, 1995, and (II) with respect to which an election under this section is in effect for the corporation's taxable year which includes October 13, 1995, or
  - ⚭ (ii) which acquired all of the assets of a trade or business of a corporation which -
  - ⚭ (I) satisfied the requirements of subclause (I) of clause
  - ⚭ (i) with respect to such trade or business, and (II) satisfied the requirements of subclause (II) of clause (i).
  - ⚭ (B) New lines of business prohibited If, after October 13, 1995, a corporation which would (but for this subparagraph) be an existing credit claimant adds a substantial new line of business (other than in an acquisition described in subparagraph (A)(ii)), such corporation shall cease to be treated as an existing credit claimant as of the close of the taxable year ending before the date of such addition.
  - ⚭ (C) Binding contract exception If, on October 13, 1995, and at all times thereafter, there is in effect with respect to a corporation a binding contract for the acquisition of assets to be used in, or for the sale of assets to be produced from, a trade or business, the corporation shall be treated for purposes of this paragraph as actively conducting such trade or business on October 13, 1995. The preceding sentence shall not apply if such trade or business is not actively conducted before January 1, 1996.
  - ⚭ (10) Separate application to each possession For purposes of determining -
  - ⚭ (A) whether a taxpayer is an existing credit claimant, and (B) the amount of the credit allowed under this section, this subsection (and so much of this section as relates to this subsection) shall be applied separately with respect to each possession.

#### Footnotes

[1] So in original. Probably should be "corporation's".

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