

of governmental financial or monetary policy if the primary purpose for holding the instrument is to implement or effectuate such policy.

(ii) *Illustration.* The following example illustrates the application of this paragraph (a)(5).

Example. In order to ensure sufficient currency reserves, the monetary authority of foreign country FC issues short-term government obligations. The amount received from the obligations is invested in U.S. financial instruments. Since the primary purpose for obtaining the U.S. financial instruments is to implement FC's monetary policy, the income received from the financial instruments is exempt from taxation under section 892.

(b) *Illustrations.* The principles of paragraph (a) of this section may be illustrated by the following examples.

Example 1. X, a foreign corporation not engaged in commercial activity anywhere in the world, is a controlled entity of a foreign sovereign within the meaning of §1.892-2T(a)(3). X is not a Central bank of issue as defined in §1.895-1(b). In 1987, X received the following items of income from investments in the United States: (i) Dividends from a portfolio of publicly traded stocks in U.S. corporations in which X owns less than 50 percent of the stock; (ii) dividends from BTB Corporation, an automobile manufacturer, in which X owns 50 percent of the stock; (iii) interest from bonds issued by noncontrolled entities and from interest-bearing bank deposits in noncontrolled entities; (iv) rents from a net lease on real property; (v) gains from silver futures contracts; (vi) gains from wheat futures contracts; (vii) gains from spot sales of nonfunctional foreign currency in X's possession; (viii) gains from the disposition of a publicly traded partnership interest, and (ix) gains from the disposition of the stock of Z Corporation, a United States real property holding company as defined in section 897, of which X owns 12 percent of the stock. Only income derived from sources described in paragraph (a)(1) of this section is treated as income of a foreign government eligible for exemption from taxation. Accordingly, only income received by X from items (i), (iii), (v) provided that the silver futures contracts are held in the execution of governmental financial or monetary policy, and (ix) is exempt from taxation under section 892.

Example 2. The facts are the same as in *Example 1*, except that X is also a central bank of issue within the meaning of section 895. Since physical possession of nonfunctional foreign currency when held by a central bank of issue is considered a financial instrument, the item (vii) gains from spot sales of

nonfunctional foreign currency are exempt from taxation under paragraph (a)(1) of this section, if physical possession of the currency was an essential part of X's reserve policy in the execution of its governmental financial or monetary policy.

Example 3. State Concert Bureau, an integral part of a foreign sovereign within the meaning of §1.892-2T(a)(2), entered into an agreement with a U.S. corporation engaged in the business of promoting international cultural programs. Under the agreement the State Concert Bureau agreed to send a ballet troupe on tour for 5 weeks in the United States. The Bureau received approximately \$60,000 from the performances. Regardless of whether the performances themselves constitute commercial activities under §1.892-4T, the income received by the Bureau is not exempt from taxation under section 892 since the income is from sources other than described in paragraph (a)(1) of this section.

[T.D. 8211, 53 FR 24062, June 27, 1988]

§ 1.892-4T Commercial activities (temporary regulations).

(a) *Purpose.* The exemption generally applicable to a foreign government (as defined in §1.892-2T) for income described in §1.892-3T does not apply to income derived from the conduct of a commercial activity or income received by a controlled commercial entity or received (directly or indirectly) from a controlled commercial entity. This section provides rules for determining whether income is derived from the conduct of a commercial activity. These rules also apply in determining under §1.892-5T whether an entity is a controlled commercial entity.

(b) *In general.* Except as provided in paragraph (c) of this section, all activities (whether conducted within or outside the United States) which are ordinarily conducted by the taxpayer or by other persons with a view towards the current or future production of income or gain are commercial activities. An activity may be considered a commercial activity even if such activity does not constitute the conduct of a trade or business in the United States under section 864(b).

(c) *Activities that are not commercial—*
(1) *Investments—*(i) *In general.* Subject to the provisions of paragraphs (ii) and (iii) of this paragraph (c)(1), the following are not commercial activities: Investments in stocks, bonds, and other securities; loans; investments in

financial instruments held in the execution of governmental financial or monetary policy; the holding of net leases on real property or land which is not producing income (other than on its sale or from an investment in net leases on real property); and the holding of bank deposits in banks. Transferring securities under a loan agreement which meets the requirements of section 1058 is an investment for purposes of this paragraph (c)(1)(i). An activity will not cease to be an investment solely because of the volume of transactions of that activity or because of other unrelated activities.

(ii) *Trading*. Effecting transactions in stocks, securities, or commodities for a foreign government's own account does not constitute a commercial activity regardless of whether such activities constitute a trade or business for purposes of section 162 or a U.S. trade or business for purposes of section 864. Such transactions are not commercial activities regardless of whether they are effected by the foreign government through its employees or through a broker, commission agent, custodian, or other independent agent and regardless of whether or not any such employee or agent has discretionary authority to make decisions in effecting the transactions. An activity undertaken as a dealer, however, as defined in § 1.864-2(c)(2)(iv)(a) will not be an investment for purposes of this paragraph (c)(1)(i). For purposes of this paragraph (c)(1)(ii), the term "commodities" means commodities of a kind customarily dealt in on an organized commodity exchange but only if the transaction is of a kind customarily consummated at such place.

(iii) *Banking, financing, etc.* Investments (including loans) made by a banking, financing, or similar business constitute commercial activities, even if the income derived from such investments is not considered to be income effectively connected to the active conduct of a banking, financing, or similar business in the U.S. by reason of the application of § 1.864-4(c)(5).

(2) *Cultural events*. Performances and exhibitions within or outside the United States of amateur athletic events and events devoted to the pro-

motion of the arts by cultural organizations are not commercial activities.

(3) *Non-profit activities*. Activities that are not customarily attributable to or carried on by private enterprise for profit are not commercial activities. The fact that in some instances Federal, State, or local governments of the United States also are engaged in the same or similar activity does not mean necessarily that it is a non-profit activity. For example, even though the United States Government may be engaged in the activity of operating a railroad, operating a railroad is not a non-profit activity.

(4) *Governmental functions*. Governmental functions are not commercial activities. The term "governmental functions" shall be determined under U.S. standards. In general, activities performed for the general public with respect to the common welfare or which relate to the administration of some phase of government will be considered governmental functions. For example, the operation of libraries, toll bridges, or local transportation services and activities substantially equivalent to the Federal Aviation Authority, Interstate Commerce Commission, or United States Postal Service will all be considered governmental functions for purposes of this section.

(5) *Purchasing*. The mere purchasing of goods for the use of a foreign government is not a commercial activity.

[T.D. 8211, 53 FR 24063, June 27, 1988]

§ 1.892-5T Controlled commercial entity (temporary regulations).

(a) *In general*. The exemption generally applicable to a foreign government (as defined in § 1.892-2T) for income described in § 1.892-3T does not apply to income received by a controlled commercial entity or received (directly or indirectly) from a controlled commercial entity. The term "controlled commercial entity" means any entity engaged in commercial activities as defined in § 1.892-4T (whether conducted within or outside the United States) if the government—

(1) Holds (directly or indirectly) any interest in such entity which (by value or voting power) is 50 percent or more of the total of such interests in such entity, or