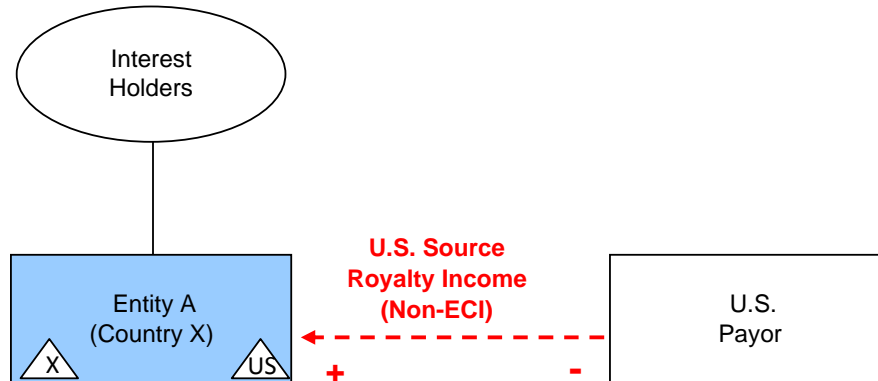
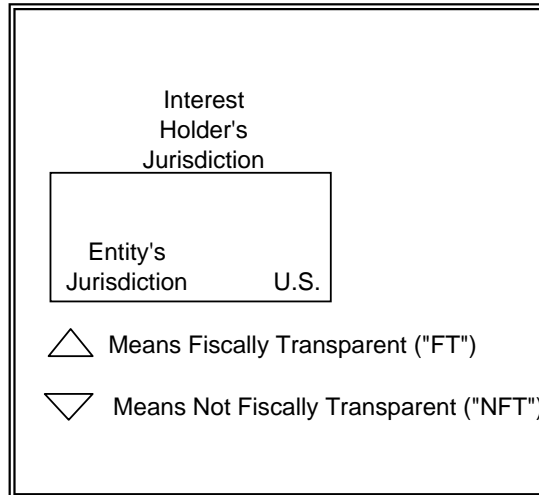


Reg. 1.894-1(d)(5), Example 1

**Fiscally Transparent ("FT")
Entity Not Eligible For
Reduced Treaty Rate**

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Key to Fiscal Transparency



Because A is fiscally transparent in Country X, A does not "derive" the income. Thus, A cannot claim a reduced treaty rate under the U.S.-X Income Tax Treaty.

Entity A is a business organization formed under the laws of Country X that has an income tax treaty in effect with the United States. A is treated as a partnership (FT) for U.S. federal income tax purposes. A is also treated as a partnership (FT) under the laws of Country X. A receives royalty income from U.S. sources that is not effectively connected with the conduct of a trade or business in the United States. A is fiscally transparent in its jurisdiction with respect to the U.S. source royalty income in Country X and, thus, A does not derive such income for purposes of the U.S.-X income tax treaty.

