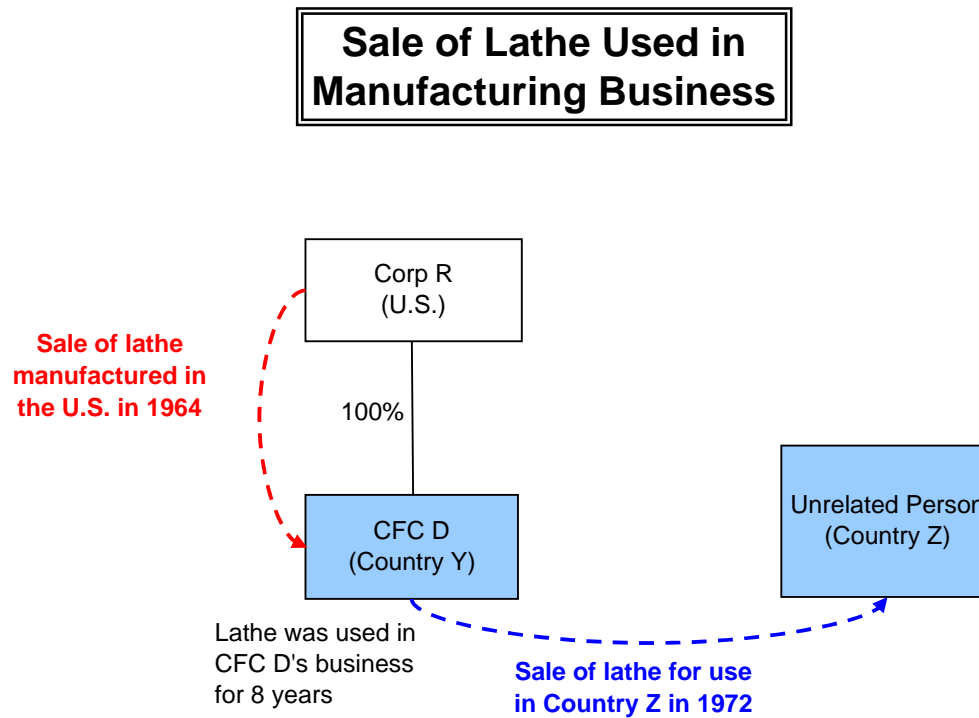


Reg. 1.954-3(a)(1)(iii), Example 4

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Controlled foreign corporation D, incorporated under the laws of foreign country Y, is a wholly owned subsidiary of domestic corporation R. In 1964, D Corporation acquires a United States manufactured lathe from R Corporation. In 1972, after having made a substantial use of the lathe in its manufacturing business, D Corporation sells the lathe to an unrelated person for use in foreign country Z. **Gross income from the sale of the lathe is not foreign base company sales income** since it is sold to an unrelated person after substantial use has been made of it by D Corporation in its business.

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