

## Reg. 1.863-7(d), Example

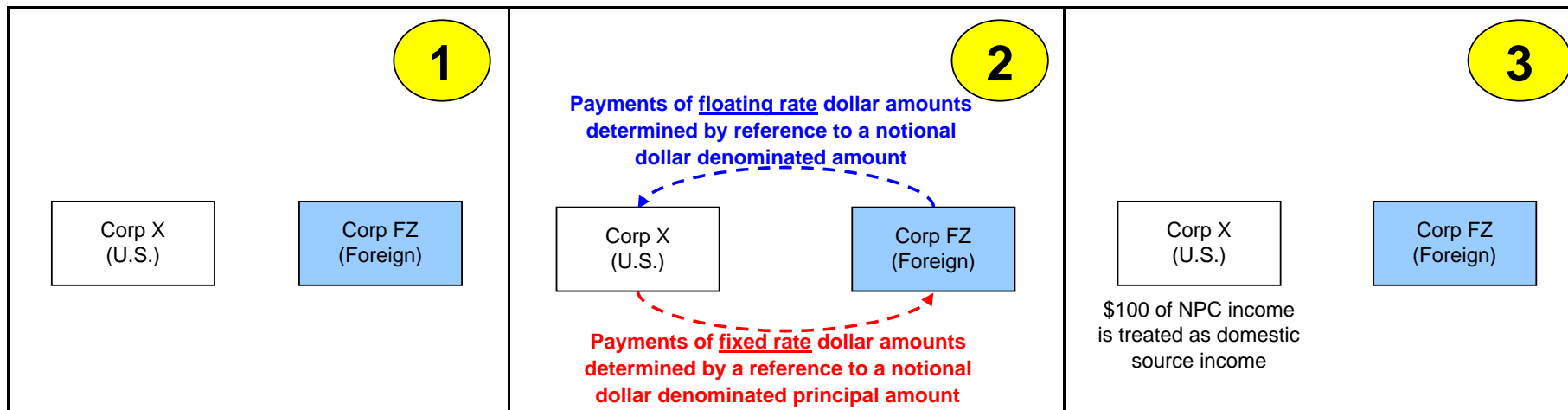
### Source of Notional Principal Contract Income

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#### Initial Structure

#### Interest Rate Swap Contract

#### Ending Point



On January 1, 1990, X, a calendar year domestic corporation, entered into an interest rate swap contract with FZ, an unrelated foreign corporation. X does not have a qualified business unit outside the United States. Under the contract, X is required to pay FZ fixed rate dollar amounts, and FZ is required to pay X floating rate dollar amounts, each determined solely by reference to a notional dollar denominated principal amount specified under the contract. The contract is a notional principal contract under Reg. 1.863-7(a) because the contract provides for the payment of amounts at specified intervals calculated by reference to a specified index upon a notional principal amount in exchange for a promise to pay similar amounts.

During 1990, X had notional principal contract income of \$100 in connection with the notional principal contract. The contract also provides that payments more than 30 days late give rise to a \$5 fee. X received such a fee in 1990. The source of notional principal contract income is generally determined by reference to the residence of the taxpayer. See Reg. 1.863-7(b)(1). The source of X's \$100 of income attributable to the swap agreement is domestic. The \$5 fee is not notional principal contract income.

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