

In general, an asset held for the principal purpose of promoting the conduct of a trade or business in the United States is to be considered held for use in such trade or business, and any income, gain, or loss derived from such asset will be treated as effectively connected with the conduct of such trade or business. The income, gain, or loss derived from an asset acquired in the ordinary course of a trade or business conducted in the United States (e.g., interest on a trade account receivable) will generally be considered derived from the activities of such trade or business and treated as effectively connected with the conduct of such trade or business.

*Example.*—F, a foreign corporation, is engaged in manufacturing operations in the United States. In order to secure a constant source of supply for its U.S. factory, F corporation purchases stock in domestic corporation N. Dividends on, and any gain realized on the disposition of, such stock will be considered income effectively connected with the conduct of the U.S. business.

If there is no direct relationship between the U.S. business and the holding of the asset, such asset will not generally be considered used in, or held for use in, such business, and the income from such asset will not be considered effectively connected with the conduct of such business. In determining whether such a direct relationship exists, consideration is to be given primarily to the connection between the asset and the needs of the U.S. business. However, also to be taken into account in applying the factors are: (1) the source of the funds or other assets which were used to acquire the asset in question; (2) the disposition of the income from such asset; and (3) the extent of management and control by the U.S. business over such asset. Generally, the presence of these three factors is to be determinative of the assets being used in the business without showing that the income or assets are needed in the U.S. business.

The significance to be attached to the disposition of the income will depend on the amount of such income and its relation to the other activities of the U.S. business. Management activities relating to an asset are to be taken into account in determining whether a particular asset is used in, or held for use in, the conduct of a trade or business within the United States only if they are significant in relation to the investments involved. Income from investment assets is not to be considered effectively connected with the conduct of a U.S. business merely because employees of that business exercise management or control over such assets.

Investment income realized by a nonresident alien individual engaged in business within the United States by reason of his performing personal services in the United States will not be treated as income effectively connected with the conduct of a trade or business within the United States, unless there is a direct economic relationship between his holding of the assets from which such income results and his business of performing the personal services. Where there is such a relationship, as for example, where such an individual purchases stock in a domestic corporation to assure the opportunity of performing personal services in the United States for such corporation, income derived from such assets may be effectively connected with his conduct of such business within the United States.