DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR

FROM: W. EDWARD WILLIAMS
Senior Technical Reviewer, Branch 1 CC:INTL:Br1

SUBJECT: Claim of Exclusion Under I.R.C. § 931 for Compensation Earned In Johnston Island

This Field Service Advice responds to your memorandum dated January 14, 1999, concerning the above matter. Field Service Advice is not binding on Examination or Appeals and is not a final case determination. This document is not to be used or cited
as precedent.

LEGEND:

Taxpayer =
Year 1 =
Year 2 =
Year 3 =
Year 4 =

ISSUE:

Whether income derived from rendering personal services by taxpayer ("Taxpayer") as an employee of a civilian contractor on Johnston Island during Year 4 may be excluded by the Taxpayer from his gross income under section 931(a) of the Internal Revenue Code of 1986 ("I.R.C.") ?

CONCLUSION:

Based on the facts presented, we conclude that the Taxpayer is not entitled to claim the I.R.C. § 931 exclusion, because Johnston Island is not a "specified possession" as defined in I.R.C. § 931(c).

Taxpayer is an individual U.S. citizen who was employed during Year 4 by a civilian contractor performing U.S. government contracts on Johnston Island. There is no information provided regarding the amount of income earned by the Taxpayer during Years 1 through 4, or the location of his employment during Years 1 through 3. The Taxpayer states that on his income tax return (Form 1040) for Year 4, he claimed the I.R.C. § 931 exclusion for compensation earned in Johnston Island. He also states that some IRS representatives have informed him that he is not entitled to claim the I.R.C. § 931 exclusion

Johnston Island is a 625 acre island, and it is the largest of several islands constituting the island group known as the "Johnston Atoll", located approximately 700 nautical miles southwest of Hawaii. Johnston Island is an unincorporated territory of the United States. It was designated as a Naval Defensive Sea Area and Airspace reservation on February 14, 1941 by Executive Order 8682. It is currently operated and maintained by Field Command, Defense Special Weapons Agency (DAWA), Kirkland Air Force Base, New Mexico. In the early 1970s, the military began moving chemical weapons from Okinawa to Johnston Island, and the island became a major storage facility for U.S. chemical weapons.

In the late 1980s, the U.S. Defense Department began construction of an incinerator facility to destroy the chemical weapons on the island. Testing of the facility began in 1990, with full-scale operations beginning in 1993, with the participation of private sector contractors such as Taxpayer's employer during Year 4. Years 1 through 4 are all calendar years subsequent to 1990.

LAW AND ANALYSIS:

I.R.C. § 931 provides in pertinent part as follows:

(a) General rule.-In the case of an individual who is a bona fide resident of a specified possession during the entire taxable year, gross income shall not include -

(1) income derived from sources within any specified possession, and

> (2) income effectively connected with the conduct of a trade or business by such individual within any specified possession.
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> ***
>
> (c) Specified possession.-For purposes of this section, the term ''specified possession'' means Guam, American Samoa, and the Northern Mariana Islands.

I.R.C. § 931(a) states that the exclusion under that subsection is available only to "an individual who is a bona fide resident of a *specified possession.* [Emphasis added.]" A "specified possession" is defined by I.R.C. § 931(c) as "Guam, American Samoa, and the Northern Mariana Islands." Thus, the I.R.C. § 931 exclusion may not be claimed by the Taxpayer, because Johnston Island is not a "specified possession" within the meaning of the statute.

Prior to the Tax Reform Act of 1986 (Pub. L. 99-514 , which enacted the Internal Revenue Code of 1986 (hereinafter "1986 Code"), I.R.C. § 931(a) of the Internal Revenue Code of 1954 (hereinafter "1954 Code"), provided an exclusion from U.S. gross income, for certain income of U.S. citizens engaged in a trade or business in a U.S. possession if such income was "derived from sources within a possession of the United States." The exclusion for possession source income that was available under section 931 of the 1954 Code was limited to individuals who could show that 80 percent or more of their gross income was derived from a U.S. possession for the three-year period immediately preceding the taxable year, and that 50 percent or more of their gross income was derived from a trade or business in such U.S. possession. The Taxpayer has not provided information regarding the amount of income he earned or the location of his employment during the three-year period immediately preceding Year 4. This omission is somewhat academic because it is clear that the 1954 Code provisions do not apply to Year 4.

Section 931 of the 1954 Code did not define the term "U.S. possession." Treas. Reg. § 1.931-1, promulgated under the 1954 Code, lists various possessions of the United States, including Johnston Island, that were considered to be "possessions of the United States " for purposes of section 931 of the 1954 Code. The Tax Reform Act of 1986 generally amended the provisions of prior section 931, including the addition of a definition of the term "specified possession" in subsection (c). Since it is not included in this definition of "specified possession", Johnston Island is no longer a possession for purposes of I.R.C. § 931, regardless of the regulation issued under the 1954 Code.

Thus, neither the regulation nor the prior Code section are applicable to the time period when the Taxpayer worked on Johnston Island. The effective date provisions of the Tax Reform Act of 1986, (Section 1277 of Pub. L. 99-514.) clearly indicate that the amended section 931, under the 1986 Code is to apply to taxable years beginning after December 31, 1986. Thus, Taxpayer is not entitled to claim the I.R.C. § 931 exclusion for Year 4.

[redacted]

W. EDWARD WILLIAMS
Senior Technical Reviewer, Branch 1
Office of Associate Chief Counsel (International)