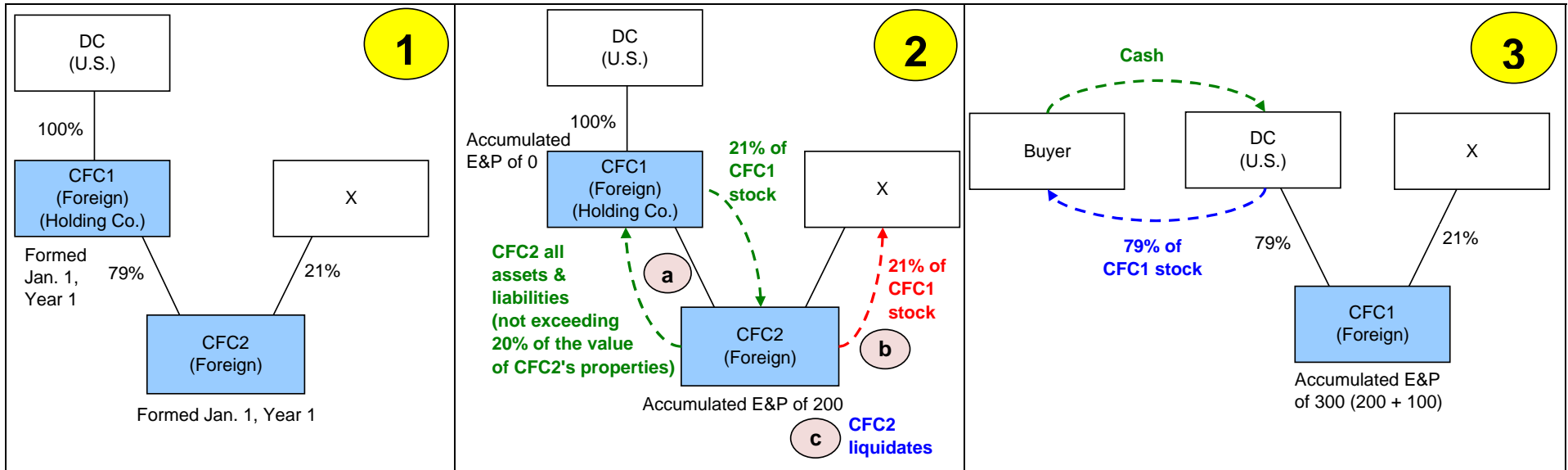


Section 1248 Gain - Sale After Upstream C Reorganization

**Upstream C Reorganization
(Dec. 31, Year 1)**

Initial Structure

Sale of CFC (Dec. 31, Year 3)



DC, a domestic corporation, has owned all the stock of CFC1, a controlled foreign corporation, since its formation on January 1, year 1. CFC1 is a holding company that has owned 79% of the stock of CFC2, a controlled foreign corporation, since its formation on January 1, year 1. The other 21% of CFC2 stock is owned by X, an unrelated party. On December 31, year 1, CFC2 has \$200 of earnings and profits. On December 31, year 1, CFC1 has no accumulated earnings and profits. On December 31, year 1, pursuant to a restructuring transaction described in section 368(a)(1)(C), CFC2 transfers all its properties to CFC1. In exchange, CFC1 assumes the liabilities of CFC2 and transfers to CFC2 voting stock representing 21% of the stock of CFC1. CFC2 distributes the voting stock to X and liquidates. The liabilities assumed do not exceed 20% of the value of the properties of CFC2. From January 1, year 2, to December 31, year 3, CFC1 accumulates \$100 of earnings and profits. On December 31, year 3, DC sells its CFC1 stock.

There is \$237 of earnings and profits attributable to DC's CFC1 stock. This amount consists of 79% of CFC2's \$200 of earnings and profits accumulated before the restructuring transaction (see section 1248(c)(2)), and 79% of CFC1's \$100 of earnings and profits accumulated after the restructuring transaction.

Ending Point

