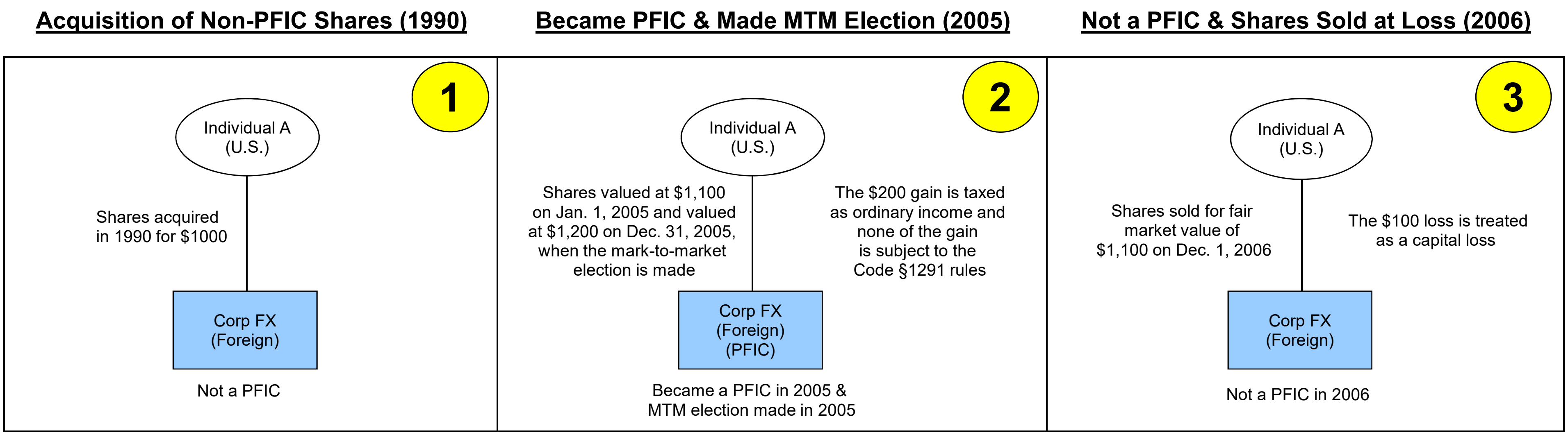
Reg. 1.1296-1(c)(7), Ex. 4

Loss Recognized in Year Ceased to be a PFIC Was Long-Term Capital Loss



A, a United States individual, purchases stock in FX, a foreign corporation that is not a PFIC, in 1990 for $1,000. On January 1, 2005, when the fair market value of the FX stock is $1,100, FX becomes a PFIC. A makes a timely Code §1296 election for taxable year 2005. On December 31, 2005, the fair market value of the FX stock is $1,200. For taxable year 2005, A includes $200 of mark to market gain (the excess of the fair market value of FX stock ($1,200) over A's adjusted basis ($1,000)) in gross income as ordinary income and pursuant to Treas. Reg. §1.1296-1(d)(1) increases his basis in the FX stock by that amount.

For taxable year 2006, FX does not satisfy either the asset test or the income test of Code §1297(a). On December 1, 2006, A sells the stock in FX for $1,100. Accordingly, for taxable year 2006, A recognizes a loss on the sale of the FX stock of $100, (the fair market value of the FX stock ($1,100) minus A's adjusted basis ($1,200) in the stock). A's $100 loss from the sale of the FX stock is treated as long-term capital loss because at the time of the sale of the FX stock by A FX did not qualify as a PFIC, and, therefore, the FX stock was not Code §1296 stock at the time of the disposition. Further, A's holding period in the FX stock for non-PFIC purposes was more than one year.