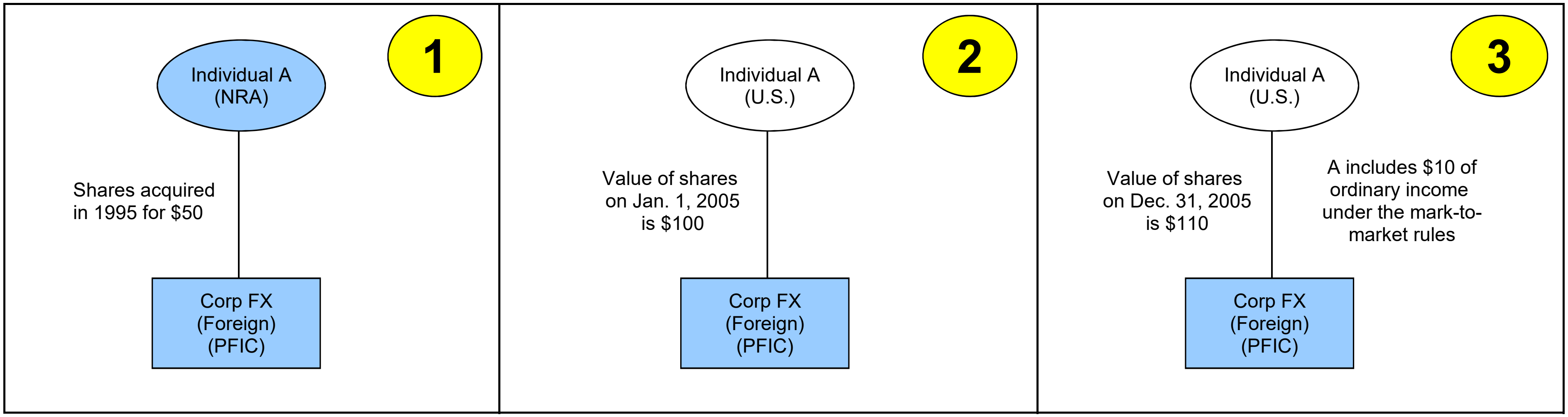
Reg. 1.1296-1(d)(5)(ii), Ex.

Pre-Residency PFIC Share Acquisition With a MTM Election in First Year of U.S. Residency

PFIC Purchase While NRA (1995) | **Becomes a Res. Alien (Jan. 2005)** | **MTM Election (2005)**



A, an NRA, purchases marketable stock in FX, a PFIC, for $50 in 1995. On January 1, 2005, A becomes a U.S. person and makes a timely Code §1296 election with respect to the stock in accordance with Treas. Reg. §1.1296-1(h). The fair market value of the FX stock on January 1, 2005, is $100. The fair market value of the FX stock on December 31, 2005, is $110. Under Treas. Reg. §1.1296-1(d)(5)(i), A computes the amount of mark to market gain or loss for the FX stock in 2005 by reference to an adjusted basis of $100, and therefore A includes $10 in gross income as mark to market gain under Treas. Reg. §1.1296-1(c)(1). Additionally, under Treas. Reg. §1.1296-1(d)(1), A's adjusted basis in the FX stock for purposes of this section is increased to $110 (and to $60 for all other tax purposes). A sells the FX stock in 2006 for $120. For purposes of applying Code §1001, A must use its original basis of $50, with any adjustments under Treas. Reg. §1.1296-1(d)(1), $10 in this case, and therefore A recognizes $60 of gain. Under Treas. Reg. §1.1296-1(c)(2) (which is applied using an adjusted basis of $110), $10 of such gain is treated as ordinary income. The remaining $50 of gain from the sale of the FX stock is long term capital gain because A held such stock for more than one year.

Sale of 1296 Stock (2006)