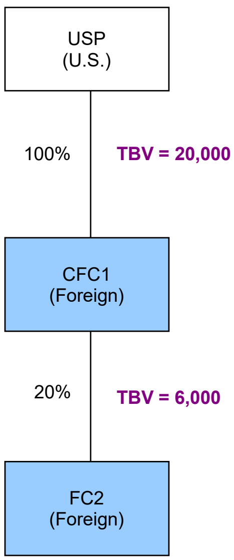
Reg. 1.861-13(c)(2), Example 2

Characterization of CFC Stock: Asset Method With One CFC & One 10/50 Corporation



A noncontrolled 10-percent owned foreign corporation (a.k.a. a 10/50 corporation)

Step 3 is skipped because none of the income is resourced under a treaty.

	Step 1			Step 2		Step 4		Step 5					
								General		Passive		951A	
CFC1 assets	Assets	Consol'd Amounts	TBV Alloc'd	Incl'n Percent-age	951A Category	General Category	Passive Category	245A Subgroup	Non-245A Subgroup	245A Subgroup	Non-245A Subgroup	245A Subgroup	Non-245A Subgroup
Tested (general)	4,000	4,000	5,000	70%	3,500	1,500		1,500					3,500
SubF (general)	1,000	7,000	8,750			8,750			8,750				
Specified (general)	3,000	3,000	3,750			3,750		3,750					
SubF (passive)	2,000	2,000	2,500				2,500				2,500		
FC2 SubF (general)	6,000												
Total	16,000	16,000	20,000		3,500	14,000	2,500	5,250	8,750	0	2,500	0	3,500

$\underbrace{\text{Step 2 and Step 4 totals}}_{20,000}$ $\underbrace{\text{Step 5 totals}}_{20,000}$

FC2 assets	Assets	TBV Alloc'd
Specified (general)	3,000	6,000
Total	3,000	6,000

Although these assets generate specified foreign source general category income, dividends from FC2 to CFC1 would be subpart F income to CFC1. Thus, CFC1 characterizes the tax book value (TBV) of the shares of FC2 as a SubF (general) asset.

USP, a domestic corporation, directly owns all of the stock of a controlled foreign corporation, CFC1. The tax book value of CFC1's stock is $20,000x. USP uses the asset method described in Reg. 1.861-12T(c)(3)(ii) to characterize the stock of CFC1. USP's inclusion percentage is 70%.

CFC1 owns the following assets with the following values as determined under Reg. 1.861-9(g)(2) and Reg. 1.861-9T(g)(3): Assets that generate income described in the foreign source gross tested income statutory grouping within the general category ($4,000x), assets that generate income described in the foreign source gross subpart F income statutory grouping within the general category ($1,000x), assets that generate specified foreign source general category gross income ($3,000x), and assets that generate income described in the foreign source gross subpart F income statutory grouping within the passive category ($2,000x).

CFC1 also owns all of the stock of FC2, a noncontrolled 10-percent owned foreign corporation. The tax book value of CFC1's stock in FC2 is $6,000x. FC2 owns the following assets with the following values as determined under Reg. 1.861-9(g)(2) and Reg. 1.861-9T(g)(3): Assets that generate specified foreign source general category gross income ($3,000x). All of the assets of FC2 generate income that, if distributed to CFC1 as a dividend, would be foreign source gross subpart F income in the general category to CFC1.