

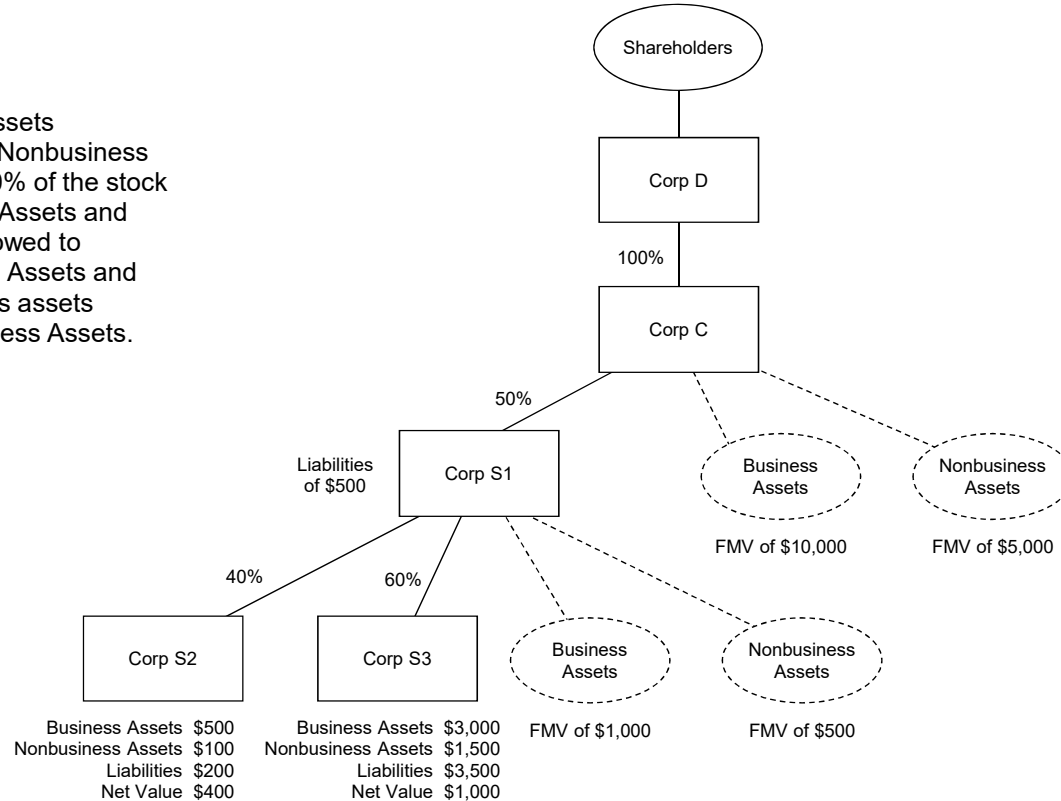
**Prop. Reg. 1.355-2(d)(4)  
Example 5**

**Nonbusiness Asset Percentage  
(50-Percent-Owned Group)**

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C's assets consist of 50% of the stock of S1 and other assets consisting of \$10,000 of Business Assets and \$5,000 of Nonbusiness Assets. S1's assets consist of 40% of the stock of S2, 60% of the stock of S3 and other assets consisting of \$1,000 of Business Assets and \$500 of Nonbusiness Assets. S1 has \$500 of liabilities, owed to unrelated persons. S2's assets consist of \$500 Business Assets and \$100 Nonbusiness Assets. S2 has \$200 of liabilities. S3's assets consist of \$3,000 Business Assets and \$1,500 Nonbusiness Assets. S3 has \$3,500 of liabilities, owed to unrelated persons.

Because C owns at least 50% of the stock of S1, S1 is a member of C's 50-Percent-Owned Group. In determining the amount of C's Business Assets and Nonbusiness Assets, whether S1's stock in S2 and S3 are Nonbusiness Assets or partially Nonbusiness Assets and partially Business Assets must first be determined. The fair market value of S1's stock in S2 is \$160 (40% of \$400 (\$500 + \$100 - \$200)). Because S1 owns less than 50% of the stock of S2, S2 is not a member of C's 50-Percent-Owned Group, and thus the S2 stock is a \$160 Nonbusiness Asset in the hands of S1.



The fair market value of S1's stock in S3 is \$600 (60% of \$1,000 (\$3,000 + \$1,500 - \$3,500)). Because C owns at least 50% of the stock of S1 and S1 owns at least 50% of the stock of S3, S3 is a member of C's 50-Percent-Owned Group. Thus, the fair market value of the S3 stock is allocated between Business Assets and Nonbusiness Assets in the same proportion as S3's proportion of Business Assets and Nonbusiness Assets. Because S3 has Business Assets of \$3,000 and Nonbusiness Assets of \$1,500, this proportion is 66 2/3% Business Assets (\$3,000/\$4,500) and 33 1/3% Nonbusiness Assets (\$1,500/\$4,500). The \$600 fair market value of S1's stock in S3 is allocated \$400 to Business Assets (\$600 x 66 2/3%) and \$200 to Nonbusiness Assets (\$600 x 33 1/3%). Thus, S1's assets consist of \$1,400 of Business Assets (\$1,000 held directly + \$400 allocated from S3) and \$860 of Nonbusiness Assets (\$500 held directly + \$160 fair market value of its S2 stock + \$200 allocated from S3).

The fair market value of C's stock in S1 is \$880 (50% of \$1,760 (\$160 + \$600 + \$1,000 + \$500 - \$500)). Because C owns at least 50% of the stock of S1, S1 is a member of C's 50-Percent-Owned Group. Thus, the fair market value of the S1 stock is allocated between Business Assets and Nonbusiness Assets in the same proportion as the proportion of S1's Business Assets and Nonbusiness Assets. Because S1 has Business Assets of \$1,400 and Nonbusiness Assets of \$860, this proportion is 61.95% Business Assets (\$1,400/\$2,260) and 38.05% Nonbusiness Assets (\$860/\$2,260). The \$880 fair market value of C's S1 stock is allocated \$545 to Business Assets (\$880 x 61.95%) and \$335 to Nonbusiness Assets (\$880 x 38.05%). Thus, C's assets consist of \$10,545 of Business Assets (\$10,000 + \$545) and \$5,335 of Nonbusiness Assets (\$5,000 + \$335), for Total Assets of \$15,880. C's Nonbusiness Asset Percentage is 33.6% (\$5,335/\$15,880).