



DC1 is a domestic corporation wholly owned by Individual A. DC1 has a \$200x value. FA is a foreign corporation wholly owned by Individual B. The value of B's FA stock is \$400x. Individual C holds a warrant to acquire FA stock from FA at an exercise price of \$20x.

Individual A transfers all of its DC1 stock to FA in exchange solely for FA stock with a value of \$200x. At the time of the transfer, the FA stock that individual C can acquire pursuant to the warrant has a \$70x value.

Under Treas. Reg. §1.7874-2(h)(1), for purposes of Code §7874, individual C is treated as owning FA stock with a \$50x value. This amount represents individual C's claim on the equity of FA after the domestic entity acquisition (\$70x value of FA stock that may be acquired pursuant to the warrant, less the \$20x exercise price), without taking into account the \$20x individual C would be required to provide to FA upon the exercise of the warrant. Thus, for purposes of Code §7874, the value of the stock of FA immediately after the transaction is \$650x (\$600x of FA stock, plus C's \$50x claim on the equity of FA). C's warrant is not taken into account for purposes of determining the voting power of FA under Code §7874.