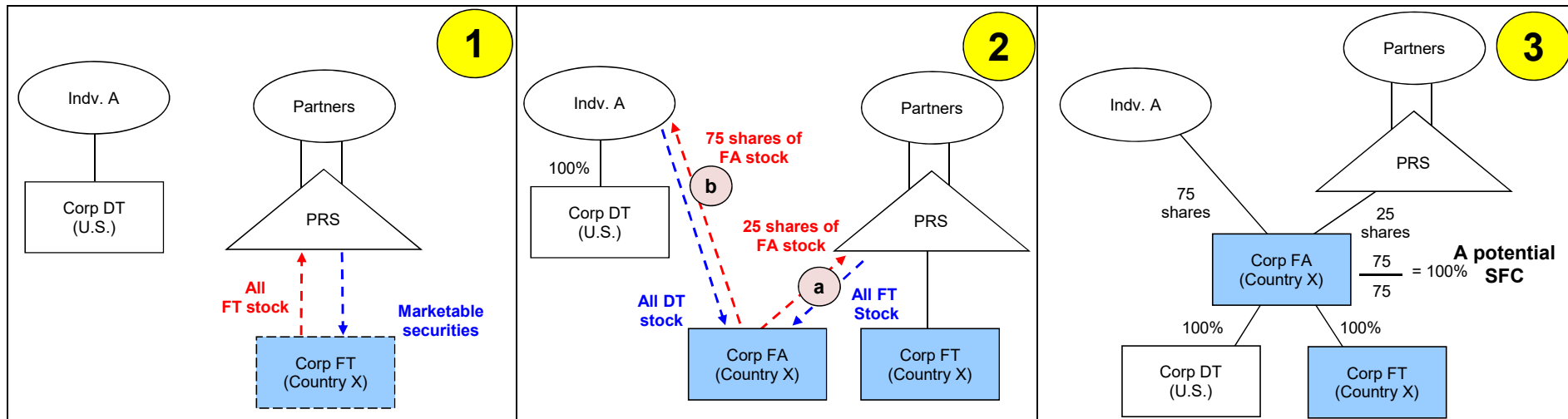


Formation of Corp FT

Stock Acquisition

Ending Point



Individual A wholly owns DT, a domestic corporation. PRS, a partnership with individual partners, transfers marketable securities (within the meaning of Treas. Reg. §1.7874-4T(i)(6)) to FT, a newly formed foreign corporation, in exchange solely for all the FT stock. Then PRS transfers the FT stock to FA, a newly formed foreign corporation, in exchange solely for 25 shares of FA stock. Finally, Individual A transfers all the DT stock to FA in exchange solely for 75 shares of FA stock. FA acquires the FT stock with a principal purpose of avoiding the purposes of Code §7874.

Under Treas. Reg. §1.7874-4T(i)(7)(iv), the FT stock constitutes nonqualified property because a principal purpose of FA acquiring the FT stock is to avoid the purposes of Code §7874. Accordingly, the 25 shares of FA stock transferred by FA to PRS in exchange for the FT stock constitute disqualified stock described in Treas. Reg. §1.7874-4T(c)(1) by reason of Treas. Reg. §1.7874-4T(c)(1)(i). Treas. Reg. §1.7874-4T(c)(2) does not reduce the amount of disqualified stock described in Treas. Reg. §1.7874-4T(c)(1)(i) because the transfer of FA stock in exchange for the FT stock increases the fair market value of FA's assets by the fair market value of the FT stock. Under Treas. Reg. §1.7874-4T(b), the 25 shares of FA stock transferred to PRS are not included in the denominator of the ownership fraction. Furthermore, even in the absence of Treas. Reg. §1.7874-4T(i)(7)(iv), the transfer of marketable securities to FT would be disregarded pursuant to Code §7874(c)(4). Accordingly, the only FA stock included in the ownership fraction is FA stock transferred to Individual A in exchange for the DT stock, and that FA stock is included in both the numerator and the denominator of the ownership fraction. Thus, the ownership fraction is 75/75.