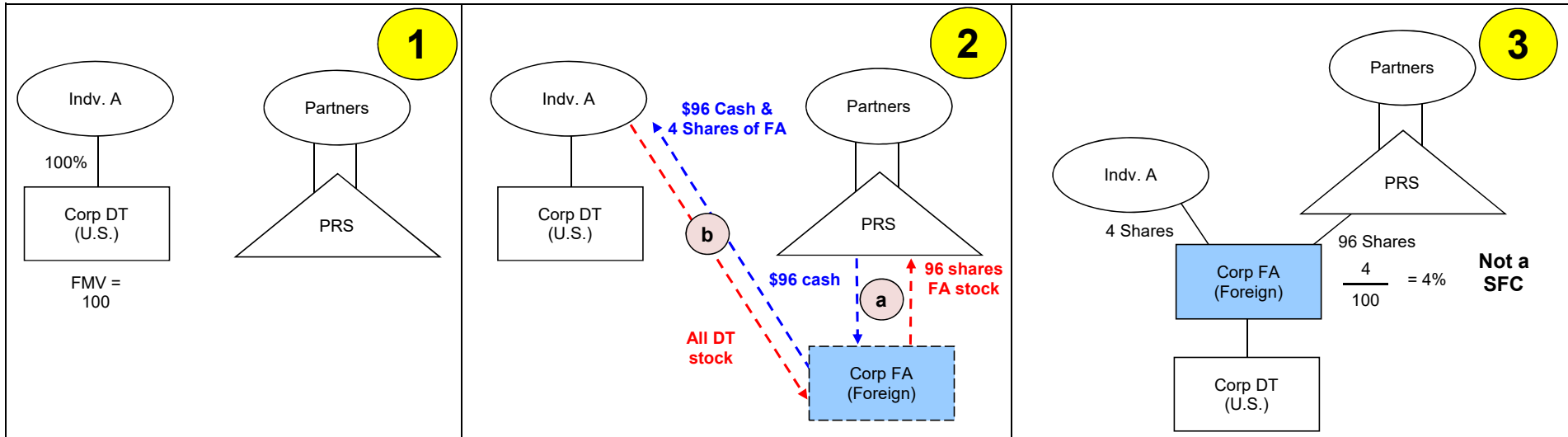


**Initial Structure**

**Cash & Stock Transfers**

**Ending Point**



Individual A wholly owns DT, a domestic corporation. The fair market value of the DT stock is \$100x. PRS, a partnership with individual partners, transfers \$96x of cash to FA, a newly formed foreign corporation, in exchange solely for 96 shares of FA stock. Then Individual A transfers the DT stock to FA in exchange for \$96x of cash and 4 shares of FA stock.

Under Treas. Reg. §1.7874-4T(i)(7)(i), cash constitutes nonqualified property. Accordingly, the 96 shares of FA stock transferred by FA to PRS in exchange for \$96x of cash constitute disqualified stock described in Treas. Reg. §1.7874-4T(c)(1) by reason of Treas. Reg. §1.7874-4T(c)(1)(i). Furthermore, 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 \$96x of cash increases the fair market value of the assets of FA by \$96x. However, without regard to the application of Treas. Reg. §1.7874-4T(b) and Treas. Reg. §§1.7874-7T(b) and -10T(b), the ownership percentage described in Code §7874(a)(2)(B)(ii) would be less than 5% (by vote and value), or 4% (4/100, or 4 shares of FA stock held by Individual A by reason of owning the DT stock, determined under Treas. Reg. §1.7874-2(f)(2), over 100 shares of FA stock outstanding after the acquisition). Furthermore, after the acquisition and all transactions related to the acquisition, Individual A owns less than 5% (by vote and value) of the stock of FA and DT (the members of the expanded affiliated group that includes FA). Accordingly, the de minimis exception in Treas. Reg. §1.7874-4T(d)(1) applies and therefore Treas. Reg. §1.7874-4T(b) does not apply to exclude the FA stock transferred to PRS from the denominator of the ownership fraction. Therefore, the FA stock transferred to Individual A and PRS is included in the denominator of the ownership fraction. Thus, the ownership fraction is 4/100.