A, an individual, is a citizen of the United States. On January 1, 1980, B, a nonresident alien individual in foreign country FC, set up foreign corporation FX. B funded FX with 100,000x dollars and received in return all of the authorized stock of FX. A then paid B 70,000x dollars for an option to purchase all the FX stock. The option may be exercised at A's discretion at any time. The price payable by A under the option is 30,000x dollars.

After its formation FX used the 100,000x dollars with which it was capitalized to invest in stock and securities of corporations. All income received by FX during 1980 was foreign personal holding company income within the meaning of section 553. FX did not distribute any of its income, but reinvested it in additional stocks and securities of corporations. The constructive ownership rule of section 554(a)(3) provides that, if A has an option to acquire stock, then that stock will be considered as owned by A. However, section 551(a) applies only to those United States shareholders who actually own stock of the foreign personal holding company.

It has long been a principle of federal tax law that the substance of a transaction and not its form will determine the federal income tax consequences of the transaction. Commissioner v. Court Holding Company, 324 U.S. 331 (1945), Rev. Rul. 61-18. In form, A acquired an option to purchase for 30,000x dollars an asset worth 100,000x dollars. Stock, which represents the ownership or equity of a corporation, is a risk investment and to purchase stock means to assume the risks of an investor in equity. See John Kelley Co. v. Commissioner, 326 U.S. 521, 530 (1946); Zilkha and Sons, Inc. v. Commissioner, 52 T.C. 607, 613 (1969), acq., 1970-1 C.B. xvi. By obtaining the right to purchase for 30,000x dollars stock worth 100,000x dollars, A has assumed the risks of an investor in equity. In substance, 100 percent of the funds used to capitalize FX and, hence, 100 percent of the funds at risk have been or will be furnished by A. Depending upon the success or failure of FX, it is A's investment, not that of B, that will appreciate or depreciate. A has assumed the benefits and burdens of the ownership of FX stock and, therefore, the sale of FX stock to A has been completed. See Tennessee Natural Gas Lines, Inc. and Subsidiary v. Commissioner, 71 T.C. 74, 83 (1978), acq., 1979-2 C.B. 2. Under the facts presented, A is considered the actual owner of 100 percent of the stock of FX for the entire calendar year.

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