

is illustrated by the following examples:

Example 1. A, an individual, owns 79 percent of the stock (by value) of Corporation X, and a trust for A's children owns the remaining 21 percent of the stock. A's children are deemed to own the stock owned for their benefit by the trust in proportion to their actuarial interests in the trust (section 318(a)(2)(B)). A, in turn, constructively owns the stock so deemed to be owned by his children (section 318(a)(1)(A)(ii)). Thus, A is treated as owning all the stock of Corporation X, and any gain A recognizes from the sale of depreciable property to Corporation X is treated under section 1239 as ordinary income.

Example 2. Y Corporation owns 100 percent in value of the stock of Z Corporation. Y Corporation sells depreciable property at a gain to Z Corporation. P and his daughter, D, own 80 percent in value of the Y Corporation stock. Under the constructive ownership rules of section 318, as applied to section 1239, P and D are each considered to own the stock in Z Corporation owned by Y Corporation. Also, P and D are each considered to own the stock in Y Corporation owned by the other. As a result, both P and D constructively own 80 percent or more in value of the stock of both Y and Z Corporations. Thus, the sale between Y and Z is governed by section 1239 and produces ordinary income to Y.

[T.D. 7569, 43 FR 51388, Nov. 3, 1978, as amended by T.D. 8106, 51 FR 42835, Nov. 26, 1986]

§ 1.1239-2 Gain from sale or exchange of depreciable property between certain related taxpayers on or before October 4, 1976.

Section 1239 provides in general that any gain from the sale or exchange of depreciable property between a husband and wife or between an individual and a controlled corporation on or before October 4, 1976 (and in the case of a sale or exchange occurring after that date if made under a binding contract entered into on or before that date), shall be treated as ordinary income. Thus, any gain recognized to the transferor from a sale or exchange after May 3, 1951, and on or before October 4, 1976 (or thereafter if pursuant to a binding contract entered into on or before that date), directly or indirectly, between a husband and wife or between an individual and a controlled corporation, of property which, in the hands of the transferee, is property of a character subject to an allowance for depreciation provided in section 167 (including

such property on which a deduction for amortization is allowable under sections 168 and 169) shall be considered as gain from the sale or exchange of property which is neither a capital asset nor property described in section 1231. For the purpose of section 1239, a corporation is controlled when more than 80 percent in value of all outstanding stock of the corporation is beneficially owned by the taxpayer, his spouse, and his minor children and minor grandchildren. For the purpose of this section, the terms *children* and *grandchildren* include legally adopted children and their children. The provisions of section 1239(a)(2) are applicable whether property is transferred from a corporation to a shareholder or from a shareholder to a corporation.

[T.D. 6500, 25 FR 12021, Nov. 26, 1960, as amended by T.D. 7569, 43 FR 51388, Nov. 3, 1978]

§ 1.1240-1 Capital gains treatment of certain termination payments.

Any amounts received by an employee for the assignment or release of all his rights to receive, after termination of his employment and for a period of not less than five years or for a period ending with his death, a percentage of the profits or receipts of his employer attributable to a time subsequent to such termination, are considered received from the sale or exchange of a capital asset held for more than six months if the following requirements are met:

(a) The employee was employed by the employer, in whose future profits or receipts the employee had an interest, for a period of more than 20 years before the assignment or release by the employee of his rights in such future profits or receipts,

(b) The full rights of the employee to the percentage of the future profits or receipts on such employer, which rights are the subject of the assignment or release, were incorporated in the terms of the contract of employment between the employee and the employer for a period of at least 12 years, and were so incorporated before August 16, 1954,