shall be determined without taking into account any amount attributable to a period prior to the date on which such shareholder acquired such stock. See section 1248 and the regulations thereunder for rules governing treatment of gain from sales or exchanges of stock in certain foreign corporations.

(d) *Illustrations.* The application of this section may be illustrated by the following examples:

Example 1. A, a United States shareholder, owns 60 percent of the only class of stock of M Corporation, a controlled foreign corporation throughout the entire period here involved. Both A and M Corporation use the calendar year as a taxable year. Corporation M's qualified investments in less developed countries at the close of 1964 amount to $125,000; and, at the close of 1965, to $75,000. During 1965, M Corporation realizes recognized gains of $5,000 and recognized losses of $15,000, on sales of qualified investments in less developed countries. Corporation M's earnings and profits for 1965 and its accumulated earnings and profits for 1963 and 1964 amount to $45,000, as determined under paragraph (b)(2) of this section. The amount excluded under section 954(b)(1) for 1963 from its foreign base company income is $75,000, and the amount of its previously excluded subpart F income withdrawn for 1964 from investment in less developed countries is $25,000. The amount of M Corporation's previously excluded subpart F income withdrawn for 1965 from investment in less developed countries is $40,000, and A's pro rata share of such amount is $24,000, determined as follows:

(i) Qualified investments in less developed countries at the close of 1964	$125,000
(ii) Less: Qualified investments in less developed countries at the close of 1965	75,000
(iii) Balance	50,000
(iv) Less: Excess of recognized losses over recognized gains on sales during 1965 of qualified investments in less developed countries ($15,000 less $5,000)	10,000
(v) Tentative decrease in qualified investments in less developed countries for 1965	40,000
(vi) Earnings and profits for 1963, 1964, and 1965	45,000
(vii) Excess of amount excluded under section 954(b)(1) from foreign base company income for 1963 ($75,000 over amount of previously excluded subpart F income withdrawn for 1964 from investment in less developed countries ($25,000)	50,000
(viii) M Corporation's amount of previously excluded subpart F income withdrawn for 1965 from investment in less developed countries (item (v), but not to exceed the lesser of item (vi) or item (vii))	40,000
(ix) A's pro rata share of M Corporation's amount of previously excluded subpart F income withdrawn for 1965 from investment in less developed countries (60 percent of $40,000)	$24,000

Example 2. The facts are the same as in example 1, except that M Corporation's earnings and profits (determined under paragraph (b)(2) of this section) for 1963, 1964, and 1965 (item (vi)) are $30,000 instead of $45,000. Corporation M's amount of previously excluded subpart F income withdrawn for 1965 from investment in less developed countries is $30,000. A's pro rata share of such amount is $18,000 (60 percent of $30,000).

Example 3. The facts are the same as in example 1, except that the excess of the amount excluded under section 954(b)(1) for 1963 from M Corporation's foreign base company income over the amount of its previously excluded subpart F income withdrawn for 1964 from investment in less developed countries (item (vii)) is $20,000 instead of $50,000. Corporation M's amount of previously excluded subpart F income withdrawn for 1965 from investment in less developed countries is $20,000. A's pro rata share of such amount is $12,000 (60 percent of $20,000).

[T.D. 6683, 28 FR 11178, Oct. 18, 1963, as amended by T.D. 6795, 30 FR 942, Jan. 29, 1965; T.D. 7893, 48 FR 22509, May 19, 1983; T.D. 7894, 48 FR 22529, May 19, 1983]

§ 1.955–2 Amount of a controlled foreign corporation's qualified investments in less developed countries.

(a) *Included property.* For purposes of sections 951 through 964, a controlled foreign corporation's ''qualified investments in less developed countries'' are items of property (other than property excluded under paragraph (b)(1) of this section) owned directly by such corporation on the applicable determination date for purposes of section 954(f) or section 955(a)(2) and consisting of one or more of the following:

(1) Stock of a less developed country corporation if the controlled foreign corporation owns (within the meaning of paragraph (b)(2) of this section) on the applicable determination date 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation;

(2) An obligation (as defined in paragraph (b)(3) of this section) of a less developed country corporation which, at the time of acquisition (as defined in paragraph (b)(4) of this section) of such obligation by the controlled foreign corporation, has a maturity of one year or more, but only if the controlled foreign corporation owns (within the meaning of paragraph (b)(2) of this section) on the applicable determination date 10 percent or more of the total combined voting power of all classes of stock of such less developed country corporation; and

(3) An obligation (as defined in paragraph (b)(3) of this section) of a less developed country, including obligations issued or guaranteed by the government of such country or of a political subdivision thereof and obligations of any agency or instrumentality of such country, in which such country is financially committed. The application of this subparagraph may be illustrated by the following example:

Example. A, a political subdivision of foreign country X, constructs and operates a toll bridge. Country X is a less developed country throughout the period here involved. A issues bonds under an indenture which provides for amortization of the principal and interest of such bonds only out of the net revenues derived from operation of the bridge. The bonds of A are obligations in which X country is financially committed and, in the hands of a controlled foreign corporation, are qualified investments in less developed countries.

(b) *Special rules*—(1) *Excluded property*. For purposes of paragraph (a) of this section, property which is disposed of within 6 months after the date of its acquisition shall be excluded from a controlled foreign corporation's qualified investments in less developed countries. However, the fact that property acquired by a controlled foreign corporation has not been held on an applicable determination date for more than 6 months after the date of its acquisition shall not prevent such property from being included in the controlled foreign corporation's qualified investments in less developed countries on such date. Proper adjustments shall be made subsequently, however, to exclude any item of property so included, if the property is in fact disposed of within 6 months after the date of its acquisition. See section 955(b)(4).

(2) *Determination of stock ownership*. In determining for purposes of paragraphs (a)(1) and (2) of this section whether a controlled foreign corporation owns 10 percent or more of the total combined voting power of all classes of stock of a less developed country corporation, only stock owned directly by such controlled foreign corporation shall be taken into account and the provisions of section 958 and the regulations thereunder shall not apply. See section 958(a)(1).

(3) *Obligation defined*. For purposes of paragraphs (a)(2) and (3) of this section, the term ''obligation'' means any bond, note, debenture, certificate, or other evidence of indebtedness. In the absence of legal, governmental, or business reasons to the contrary, the indebtedness must bear interest or be issued at a discount.

(4) *Date of acquisition*. For purposes of paragraphs (a)(2) and (b)(5)(i) of this section, stock or an obligation shall be considered acquired by a foreign corporation as of the date such corporation acquires an adjusted basis in the stock or obligation. For this purpose, in a case in which a foreign corporation acquires stock or an obligation in a transaction (other than a reorganization of the type described in section 368(a)(1)(E) or (F)) in which no gain or loss would be recognized had the transaction been between two domestic corporations, such corporation will be considered to have acquired an adjusted basis in such stock or obligation as of the date such transaction occurs.

(5) *Taxable years beginning after December 31, 1975*. For taxable years beginning after December 31, 1975, qualified investments in less developed countries do not include—

(i) Any property acquired after the latest determination date applicable to a taxable year beginning before December 31, 1975,

(ii) Stock or obligations of a less developed country shipping company described in § 1.955–5(b), and

(iii) Stock or obligations which were not treated as qualified investments in less developed countries on the later of the two determination dates applicable to the preceding taxable year.

See § 1.955–1(b)(3) for rules relating to the application of this subparagraph. See § 1.955A–2(h) for rules relating to the treatment of investments in stock or obligations described in subdivision (ii) of this subparagraph as qualified investments in foreign base company shipping operations.

(6) *Determination dates.* For purposes of subparagraph (5) of this paragraph and § 1.955–1(b)(3), the determination dates applicable to a taxable year of a controlled foreign corporation are—

(i) Except as provided in subdivision (ii) of this subparagraph, the close of such taxable year and the close of the preceding taxable year, and

(ii) With respect to a United States shareholder who has made an election under section 955(b)(3) to determine such corporation's increase in qualified investments in less developed countries at the close of the following taxable year, the close of such taxable year and the close of the taxable year immediately following such taxable year.

(c) *Termination of designation as a less developed country.* For purposes of sections 951 through 964, property which would constitute a qualified investment in a less developed country but for the fact that a foreign country or United States possession has, after the acquisition of such property by the controlled foreign corporation, ceased to be a less developed country shall be treated as a qualified investment in a less developed country. The application of this paragraph may be illustrated by the following example:

Example. On December 31, 1969, in accordance with the provisions of § 1.955–4, the designation of the foreign country X as an economically less developed country is terminated. Corporation M, a controlled foreign corporation, has $50,000 of qualified investments in country X acquired before December 31, 1969. After 1969 such investments are treated as qualified investments in a less developed country notwithstanding the termination of the status of X Country as an economically less developed country. However, if such qualified investments of M Corporation are reduced to $40,000, each United States shareholder of M Corporation is required, subject to the provisions of § 1.955–1, to include his pro rata share of the $10,000 decrease in his gross income under section 951(a)(1)(A)(ii) and the regulations thereunder.

(d) *Amount attributable to property*—(1) *General rule.* For purposes of this section, the amount taken into account with respect to any property which constitutes a qualified investment in a less developed country shall be its adjusted basis as of the applicable determination date, reduced by any liability (other than a liability described in subparagraph (2) of this paragraph) to which such property is subject on such date. To be taken into account under this subparagraph, a liability must constitute a specific charge against the property involved. Thus, a liability evidenced by an open account or a liability secured only by the general credit of the controlled foreign corporation will not be taken into account. On the other hand, if a liability constitutes a specific charge against several items of property and cannot definitely be allocated to any single item of property, the liability shall be apportioned against each of such items of property in that ratio which the adjusted basis of such item on the applicable determination date bears to the adjusted basis of all such items at such time. A liability in excess of the adjusted basis of the property which is subject to such liability shall not be taken into account for the purpose of reducing the adjusted basis of other property which is not subject to such liability.

(2) *Excluded charges.* For purposes of subparagraph (1) of this paragraph, a specific charge created with respect to any item of property principally for the purpose of artificially increasing or decreasing the amount of a controlled foreign corporation's qualified investments in less developed countries will not be recognized; whether a specific charge is created principally for such purpose will depend upon all the facts and circumstances of each case. One of the factors that will be considered in making such a determination with respect to a loan is whether the loan is from a related person, as defined in section 954(d)(3) and paragraph (e) of § 1.954–1.

(3) *Statement required.* If for purposes of this section a United States shareholder of a controlled foreign corporation reduces the adjusted basis of property which constitutes a qualified investment in a less developed country

on the ground that such property is subject to a liability, he shall attach to his return a statement setting forth the adjusted basis of the property before the reduction and the amount and nature of the reduction.

(4) *Taxable years beginning after December 31, 1975.* For taxable years beginning after December 31, 1975, the amount taken into account under subparagraph (1) of this paragraph with respect to any property which constitutes a qualified investment in less developed countries shall not exceed the amount taken into account with respect to such property at the close of the preceding taxable year.

[T.D. 6683, 28 FR 11179, Oct. 18, 1963, as amended by T.D. 7894, 48 FR 22529, May 19, 1983]

§ 1.955–3 Election as to date of determining qualified investments in less developed countries.

(a) *Nature of election.* In lieu of determining the increase for a taxable year of a foreign corporation beginning before January 1, 1976, under the provisions of section 954(f) and paragraph (a) of § 1.954–5, or the decrease under the provisions of section 955(a)(2) and paragraph (b) of § 1.955–1, in a controlled foreign corporation's qualified investments in less developed countries for a taxable year in the manner provided in such provisions, a United States shareholder of such controlled foreign corporation may elect, under the provisions of section 955(b)(3) and this section, to determine such increase in accordance with the provisions of paragraph (b) of § 1.954–5 and to determine such decrease by ascertaining the amount by which—

(1) Such controlled foreign corporation's qualified investments in less developed countries at the close of such taxable year exceed its qualified investments in less developed countries at the close of the taxable year immediately following such taxable year, and reducing such excess by

(2) The amount determined under paragraph (b)(1)(ii) of § 1.955–1 for such taxable year,

subject to the limitation provided in paragraph (b)(2) of § 1.955–1 for such taxable year. An election under this section may be made with respect to each controlled foreign corporation with respect to which a person is a United States shareholder within the meaning of section 951(b), but the election may not be exercised separately with respect to the increases and the decreases of such controlled foreign corporation. If an election is made under this section to determine the increase of a controlled foreign corporation in accordance with the provisions of paragraph (b) of § 1.954–5, subsequent decreases of such controlled foreign corporation shall be determined in accordance with this paragraph and not in accordance with paragraph (b) of § 1.955–1.

(b) *Time and manner of making election*—(1) *Without consent.* An election under this section with respect to a controlled foreign corporation shall be made without the consent of the Commissioner by a United States shareholder's filing a statement to such effect with his return for his taxable year in which or with which ends the first taxable year of such controlled foreign corporation in which—

(i) Such shareholder owns, within the meaning of section 958(a), or is considered as owning by applying the rules of ownership of section 958(b), 10 percent or more of the total combined voting power of all classes of stock entitled to vote of such controlled foreign corporation, and

(ii) Such controlled foreign corporation realizes foreign base company income from which amounts are excluded under section 954(b)(1) and paragraph (b)(1) of § 1.954–1.

The statement shall contain the name and address of the controlled foreign corporation and identification of such first taxable year of such corporation. For taxable years of a foreign corporation beginning after December 31, 1975, no election under this section with respect to a controlled foreign corporation may be made without the consent of the Commissioner.

(2) *With consent.* An election under this section with respect to a controlled foreign corporation may be made by a United States shareholder at any time with the consent of the Commissioner. Consent will not be granted unless the United States shareholder and the Commissioner agree to the