

stock in the lower tier corporation while the lower tier corporation was a controlled foreign corporation, bears to (ii) the total number of days in such taxable year.

(3) *Net operating loss deduction.* For purposes of subparagraph (1) of this paragraph, the provisions of paragraph (d)(6)(iv) of this section shall not apply. In determining the amount of the net operating loss deduction for a taxable year of a lower tier corporation, the portion of a net operating loss incurred, or of taxable income earned, in a taxable year of the lower tier corporation beginning after December 31, 1962, which shall be taken into account under section 172(b)(2) shall be the amount of such loss or income (as the case may be) multiplied by the percentage described in subparagraph (2) of this paragraph for such taxable year.

[T.D. 6779, 29 FR 18139, Dec. 22, 1964, as amended by T.D. 7545, 43 FR 19653, May 8, 1978; T.D. 7728, 45 FR 72650, Nov. 3, 1980]

§ 1.1248-5 Stock ownership requirements for less developed country corporations.

(a) *General rule—(1) Requirements.* For purposes of paragraph (e)(4) of § 1.1248-3, a United States person shall be considered as satisfying the requirements of this paragraph with respect to a share (or block) of stock of a foreign corporation if on the date he sells or exchanges such share (or block):

(i) The 10-year stock ownership requirement of paragraph (b) of this section is met with respect to such share (or block), and

(ii) In the case of a United States person which is a domestic corporation, the requirement of paragraph (c) of this section, if applicable, is met.

(2) *Ownership of stock.* For purposes of this section:

(i) The rules for determining ownership of stock prescribed by section 958 (a) and (b) shall apply.

(ii) Stock owned by a United States person who is an individual, estate, or trust which was acquired by reason of the death of the predecessor in interest of such United States person shall be considered as owned by such United States persons during the period such stock was owned by such predecessor in interest, and during the period such

stock was owned by any other predecessor in interest if between such United States person and such other predecessor in interest there was no transfer other than by reason of the death of an individual.

(b) *10-year stock ownership requirement—(1) General.* A United States person meets the 10-year stock ownership requirement with respect to a share (or block) of stock in a foreign corporation which he sells or exchanges only if the share (or block) was owned (under the rules of paragraph (a)(2) of this section) by such person for a continuous period of at least 10 years ending on the date of the sale or exchange. See the first sentence of section 1248(d)(3). Thus, for example, if Jones, a United States person, sells a share of stock in a foreign corporation on January 1, 1965, the 10-year stock ownership requirement is met with respect to a share only if the share was owned (under the rules of paragraph (a)(2) of this section) by Jones continuously from January 1, 1955, to January 1, 1965. If a foreign corporation has not been in existence for at least 10 years on the date of the sale or exchange of the share, the 10-year stock ownership requirement cannot be met.

(2) *Special rule.* For purposes of this paragraph, a United States person shall be considered to have owned stock during the period he was considered to have held the stock by reason of the application of section 1223.

(c) *Disqualification of domestic corporation as a result of changes in ownership of its stock—(1) General.* (i) For purposes of paragraph (a)(1)(ii) of this section, the requirement of this paragraph must be met only if, on at least one day during the 10-year period ending on the date of the sale or exchange by a domestic corporation of a share of stock in a foreign corporation, one or more noncorporate United States shareholders (as defined in subdivision (iii) of this subparagraph) own more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the domestic corporation.

(ii) The requirement of this paragraph is that if one or more persons are noncorporate United States shareholders on the first such day (referred

to in subdivision (i) of this subparagraph), such person or persons continue after such first day, at all times during the remainder of such 10-year period, to own in the aggregate more than 50 percent of the total combined voting power of all classes of stock entitled to vote of the domestic corporation. For purposes of determining whether a domestic corporation meets the requirement of this paragraph, the stock owned by a United States person who is a noncorporate United States shareholder of a domestic corporation on such first day shall not be counted at any time after he ceases during such 10-year period to be a noncorporate United States shareholder of such corporation.

(iii) For purposes of this paragraph, the term *noncorporate United States shareholder* means, with respect to a domestic corporation, a United States person who is an individual, estate, or trust and who owns 10 percent or more of the total combined voting power of all classes of stock of such domestic corporation.

(iv) For purposes of this paragraph, the percentage of the total combined voting power of stock of a foreign corporation owned by a United States person shall be determined in accordance with the principles of section 951(b) and the regulations thereunder.

(2) *Examples.* The application of this paragraph may be illustrated by the following examples:

Example 1. During the entire period beginning December 31, 1954, and ending December 31, 1964, domestic corporation N owns all the stock of controlled foreign corporation X, a less developed country corporation. On December 31, 1964, N recognizes gain upon the sale of all its X stock. A, B, and C, who are unrelated individuals, were the only United States persons owning, or considered as owning, 10 percent or more of the total combined voting power of all classes of stock entitled to vote of N at any time during the 10-year period December 31, 1954, through December 31, 1964. The percentages of the total combined voting power in N, which A, B, and C owned during such 10-year period, are as follows:

Owner	Dec. 31, 1954-Apr. 1, 1957 (Percent)	Apr. 2, 1957-Oct. 1, 1959 (Percent)	Oct. 2, 1959-Dec. 31, 1964 (Percent)
A	20	20	20
B	9	30	30

Owner	Dec. 31, 1954-Apr. 1, 1957 (Percent)	Apr. 2, 1957-Oct. 1, 1959 (Percent)	Oct. 2, 1959-Dec. 31, 1964 (Percent)
C	30	15	9

Domestic corporation N does not meet the requirement of this paragraph with respect to the stock of controlled foreign corporation X for the following reasons:

(i) April 2, 1957, is the first day (during the 10-year period ending on December 31, 1964, the date N sells the X stock) on which noncorporate United States shareholders of N own more than 50 percent of the total combined voting power in N, and thus the requirement of this paragraph must be met. See subparagraph (1)(i) of this paragraph. Although A, B, and C did own, in the aggregate, more than 50 percent of such voting power before April 2, 1957, the voting power owned by B is not counted because B was not a noncorporate United States shareholder of N before such date.

(ii) Although C is a noncorporate United States shareholder on April 2, 1957, C ceases to own 10 percent or more of the total combined voting power in N on October 2, 1959. Thus, after October 1, 1959, the N stock which C owns is not counted for purposes of determining whether the more-than-50-percent stock ownership test is met. See subparagraph (1)(ii) of this paragraph. Accordingly, after October 1, 1959, the requirement of this paragraph is not met.

Example 2. Assume the same facts as in example (1), except that B's wife owns directly 5 percent of the total combined voting power in N from December 31, 1954, to December 31, 1964. On the basis of the assumed facts, N meets the requirement of this paragraph with respect to the stock of controlled foreign corporation X for the following reasons:

(i) December 31, 1954, is the first day (of the 10-year period ending on the date N sells the X stock) on which noncorporate United States shareholders of N own more than 50 percent of the total combined voting power in N. B is a noncorporate United States shareholder on such date because he owns, and is considered as owning, 14 percent of the total combined voting power in N (9 percent directly, and, under section 958(b), 5 percent constructively). Thus, on December 31, 1954, noncorporate United States shareholders A, B, and C own, in the aggregate, more than 50 percent of the total combined voting power in N.

(ii) A, B, and C, the noncorporate United States shareholders of N on December 31, 1954, own, and are considered as owning, more than 50 percent of the total voting power of N from December 31, 1954, to October 1, 1959. Since beginning on October 2, 1959, A owns 20 percent and B owns, and is considered as owning, 35 percent of the total

combined voting power in N, A and B owns, and are considered as owning, more than 50 percent of the total combined voting power in N from October 2, 1959, to December 31, 1964. Therefore, the requirement of this paragraph is met.

(d) *Application of section to lower tier corporation*—(1) *General.* For purposes of paragraph (g)(1)(ii) of § 1.1248-3, a United States person satisfies the requirements of this subparagraph in respect of stock of a lower tier corporation which such person, by reason of his direct ownership of the share (or block) of the first tier corporation sold or exchanged, owned within the meaning of section 958(a)(2) on the date he sold or exchanged such share (or block), if on such date:

(i) The 10-year stock ownership requirement of paragraph (b) of this section is met by such person with respect to any stock in the lower tier corporation which such person so owned, and

(ii) In the case of a United States person which is a domestic corporation, the requirement of paragraph (c) of this section, if applicable, is met.

(2) *Special rule.* For purposes of this paragraph, in applying paragraphs (b) and (c) of this section, the sale or exchange of a share (or block) of stock in a first tier corporation by a United States person shall be deemed to be the sale or exchange of any stock in a lower tier corporation which the person, by reason of his direct ownership of such share (or block) of the first tier corporation, owned within the meaning of section 958(a)(2) on the date he actually sold or exchanged such share (or block) in the first tier corporation.

[T.D. 6779, 29 FR 18142, Dec. 22, 1964]

§ 1.1248-6 Sale or exchange of stock in certain domestic corporations.

(a) *General rule.* If a United States person recognizes gain upon the sale or exchange of a share (or block) of stock of a domestic corporation which was formed or availed of principally for the holding, directly or indirectly, of stock of one or more foreign corporations, and if the conditions of paragraph (a)(2) of § 1.1248-1 would be met by such person in respect of the share (or block) if the domestic corporation were a foreign corporation, then section 1248 shall apply in respect of such gain in

accordance with the rules provided in paragraph (b) of this section.

(b) *Application.* (1) The gain referred to in paragraph (a) of this section shall be included in the gross income of the United States person as a dividend under section 1248(a) to the extent of the earnings and profits attributable under § 1.1248-2 or § 1.1248-3, whichever is applicable, to the share (or block), computed, however, in accordance with the following rules:

(i) The domestic corporation shall be treated as if it were a first tier foreign corporation;

(ii) If, after the application of subdivision (i) of this subparagraph, the provisions of paragraph (a)(3) of § 1.1248-2 or paragraph (f) of § 1.1248-3 (as the case may be) would apply in respect of a foreign corporation the stock of which is owned (within the meaning of section 958(a)) by the domestic corporation treated as the first tier corporation, such foreign corporation shall be considered a lower tier corporation;

(iii) Except to the extent provided in subdivision (iv) of this subparagraph, the earnings and profits of the domestic corporation treated as the first tier corporation accumulated for a taxable year, as computed under paragraph (d) of § 1.1248-2 or paragraph (b) of § 1.1248-3 (as the case may be), shall be considered to be zero; and

(iv) If, during a taxable year, a domestic corporation treated as the first tier corporation realizes gain upon the sale or exchange of stock in a foreign corporation, and solely by reason of the application of section 337 (relating to certain liquidations) the gain was not recognized, then the earnings and profits of such domestic corporation accumulated for the taxable year, as computed under paragraph (d) of § 1.1248-2 or paragraph (b) of § 1.1248-3 (as the case may be), shall be considered to be an amount equal to the portion of such gain realized during the taxable year which, if section 337 had not applied, would have been treated as a dividend under section 1248(a).

(2) If the person selling or exchanging the stock in the domestic corporation is an individual, the limitation on tax attributable to the amount included in his gross income as a dividend under