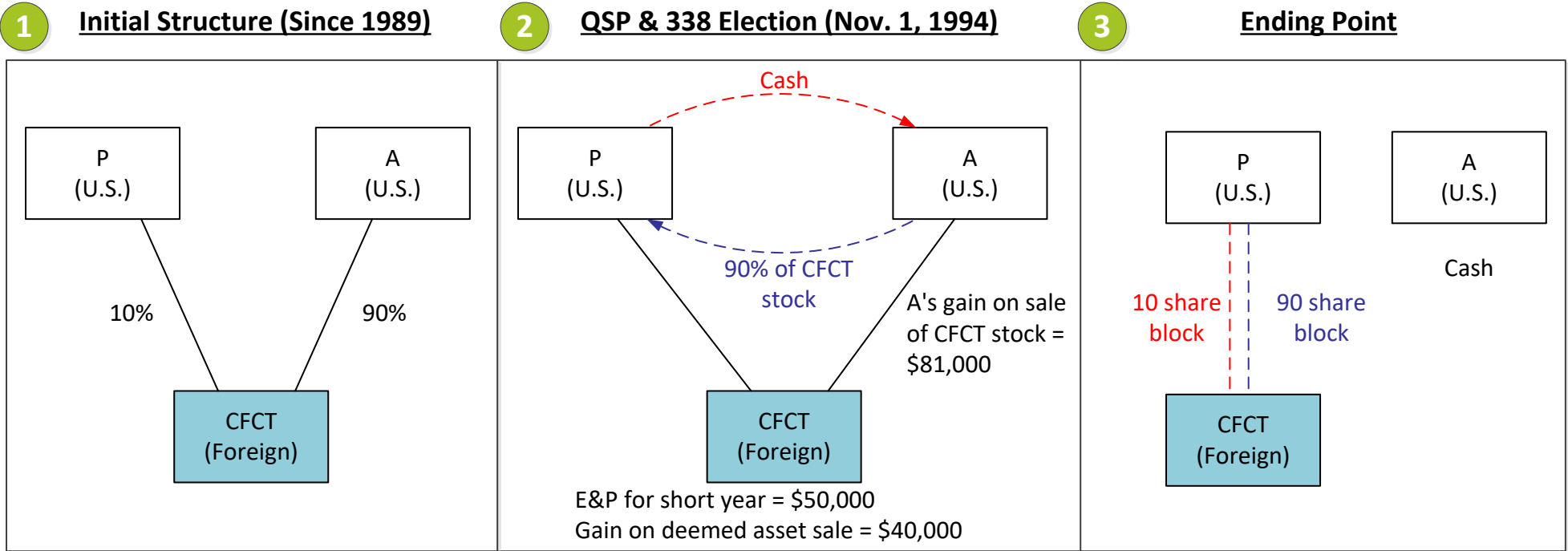


**Section 1248 Gain on QSP of a CFC Without Gain Recognition Election**



- (a)** A has owned 90 of the 100 shares of CFCT stock since CFCT was organized on March 13, 1989. P has owned the remaining 10 shares of CFCT stock since CFCT was organized. Those 10 shares constitute nonrecently purchased stock in P's hands within the meaning of section 338(b)(6)(B). On November 1, 1994, P purchases A's 90 shares of CFCT stock for \$90,000 and makes a section 338 election for CFCT. P does not make a gain recognition election under section 338(b)(3)(A) and § 1.338-5(d).
- (b)** CFCT's earnings and profits for its short taxable year ending on November 1, 1994, are \$50,000, determined without taking into account the deemed asset sale. Assume A recognizes gain of \$81,000 on the sale of the CFCT stock. Further, assume that CFCT recognizes gain of \$40,000 by reason of its deemed sale of assets under section 338(a)(1).
- (c)** A's sale of CFCT stock to P is a transfer to which section 1248 and paragraphs (b)(1) and (2) of this section apply. For purposes of applying section 1248(a) to A, the earnings and profits of CFCT for its short taxable year ending on November 1, 1994, are \$90,000 (the earnings and profits for that taxable year as determined under § 1.1248-2(e) (\$50,000) plus earnings from the deemed sale (\$40,000)). Thus, A's entire gain is characterized as a dividend under section 1248 (but see section 338(h)(16)).
- (d)** The 10 shares of nonrecently purchased CFCT stock held by P is carryover FT stock under paragraph (b)(3) of this section. Accordingly, the earnings and profits (and attributable foreign taxes) of old CFCT carry over to new CFCT solely for purposes of that block of 10 shares. The amount of old CFCT's earnings and profits taken into account with respect to that block in the event, for example, of a distribution by new CFCT with respect to that block is the amount of the section 1248 dividend that P would have recognized with respect to that block had it made a gain recognition election under section 338(b)(3)(A). Under the facts of Example 1, P would have recognized a gain of \$9,000 with respect to that block, all of which would have been a section 1248 dividend ( $\$90,000 \times 10/100$ ). Accordingly, the carryover amount for the block of 10 shares of nonrecently purchased CFCT stock is \$9,000.