

fact used to discharge or satisfy any person's legal obligation as that term is used in § 1.662(a)-4.

**§ 1.652(a)-2 Distributions in excess of distributable net income.**

If the amount of income required to be distributed currently to beneficiaries exceeds the distributable net income of the trust (as defined in section 643(a)), each beneficiary includes in his gross income an amount equivalent to his proportionate share of such distributable net income. Thus, if beneficiary A is to receive two-thirds of the trust income and B is to receive one-third, and the income required to be distributed currently is \$99,000, A will receive \$66,000 and B, \$33,000. However, if the distributable net income, as determined under section 643(a) is only \$90,000, A will include two-thirds (\$60,000) of that sum in his gross income, and B will include one-third (\$30,000) in his gross income. See §§ 1.652(b)-1 and 1.652(b)-2, however, for amounts which are not includible in the gross income of a beneficiary because of their tax-exempt character.

**§ 1.652(b)-1 Character of amounts.**

In determining the gross income of a beneficiary, the amounts includible under § 1.652(a)-1 have the same character in the hands of the beneficiary as in the hands of the trust. For example, to the extent that the amounts specified in § 1.652(a)-1 consist of income exempt from tax under section 103, such amounts are not included in the beneficiary's gross income. Similarly, dividends distributed to a beneficiary retain their original character in the beneficiary's hands for purposes of determining the availability to the beneficiary of the dividends received credit under section 34 (for dividends received on or before December 31, 1964) and the dividend exclusion under section 116. Also, to the extent that the amounts specified in § 1.652(a)-1 consist of "earned income" in the hands of the trust under the provisions of section 1348 such amount shall be treated under section 1348 as "earned income" in the hands of the beneficiary. Similarly, to the extent such amounts consist of an amount received as a part of a lump sum distribution from a quali-

fied plan and to which the provisions of section 72(n) would apply in the hands of the trust, such amount shall be treated as subject to such section in the hands of the beneficiary except where such amount is deemed under section 666(a) to have been distributed in a preceding taxable year of the trust and the partial tax described in section 668(a)(2) is determined under section 668(b)(1)(B). The tax treatment of amounts determined under § 1.652(a)-1 depends upon the beneficiary's status with respect to them not upon the status of the trust. Thus, if a beneficiary is deemed to have received foreign income of a foreign trust, the includibility of such income in his gross income depends upon his taxable status with respect to that income.

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**§ 1.652(b)-2 Allocation of income items.**

(a) The amounts specified in § 1.652(a)-1 which are required to be included in the gross income of a beneficiary are treated as consisting of the same proportion of each class of items entering into distributable net income of the trust (as defined in section 643(a)) as the total of each class bears to such distributable net income, unless the terms of the trust specifically allocate different classes of income to different beneficiaries, or unless local law requires such an allocation. For example: Assume that under the terms of the governing instrument, beneficiary A is to receive currently one-half of the trust income and beneficiaries B and C are each to receive currently one-quarter, and the distributable net income of the trust (after allocation of expenses) consists of dividends of \$10,000, taxable interest of \$10,000, and tax-exempt interest of \$4,000. A will be deemed to have received \$5,000 of dividends, \$5,000 of taxable interest, and \$2,000 of tax-exempt interest; B and C will each be deemed to have received \$2,500 of dividends, \$2,500 of taxable interest, and \$1,000 of tax-exempt interest. However, if the terms of the trust specifically allocate different classes of income to different beneficiaries, entirely or in part, or if local law requires such an allocation, each beneficiary will be deemed to have received those items of income specifically allocated to him.