

Internal Revenue Service, Treasury

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will arise by reason of a payment of income required to be distributed currently even though such income exceeds the distributable net income of the trust because the payment is an amount specified in section 661(a)(1).

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

Example 1. A trustee properly makes a distribution to a beneficiary of \$20,000 during the taxable year 1976, of which \$10,000 is income required to be distributed currently to the beneficiary. The distributable net income of the trust is \$15,000. There is an accumulation distribution of \$5,000 computed as follows.

Total distribution	\$20,000
Less: Income required to be distributed currently (section 661(a)(1))	10,000
Other amounts distributed (section 661(a)(2))	10,000
Distributable net income	\$15,000
Less: Income required to be distributed currently	10,000
Balance of distributable net income	5,000
Accumulation distribution	5,000

Example 2. Under the terms of the trust instrument, an annuity of \$15,000 is required to be paid to A out of income each year and the trustee may in his discretion make distributions out of income or corpus to B. During the taxable year the trust had income of \$18,000, as defined in section 643(b), and expenses allocable to corpus of \$5,000. Distributable net income amounted to \$13,000. The trustee distributed \$15,000 of income to A and, in the exercise of his discretion, paid \$5,000 to B. There is an accumulation distribution of \$5,000 computed as follows:

Total distribution	\$20,000
Less: Income required to be distributed currently to A (section 661(a)(1))	15,000
Other amounts distributed (section 661(a)(2))	5,000
Distributable net income	\$13,000
Less: Income required to be distributed currently to A	15,000
Balance of distributable net income	0
Accumulation distribution to B	5,000

Example 3. Under the terms of a trust instrument, the trustee may either accumulate the trust income or make distributions to A and B. The trustee may also invade corpus for the benefit of A and B. During the taxable year, the trust had income as defined in section 643(b) of \$22,000 and expenses of \$5,000 allocable to corpus. Distributable net income amounts to \$17,000. The trustee distributed \$10,000 each to A and B during the

taxable year. There is an accumulation distribution of \$3,000 computed as follows:

Total distribution	\$20,000
Less: Income required to be distributed currently	0
Other amounts distributed (section 661(a)(2))	20,000
Distributable net income	\$17,000
Less: Income required to be distributed currently	0
Balance of distributable net income	17,000
Accumulation distribution	3,000

Example 4. A dies in 1974 and bequeaths one-half the residue of his estate in trust. His widow, W, is given a power, exercisable solely by her, to require the trustee to pay her each year of the trust \$5,000 from corpus. W's right to exercise such power was exercisable at any time during the year but was not cumulative, so that, upon her failure to exercise it before the end of any taxable year of the trust, her right as to that year lapsed. The trust's taxable year is the calendar year. During the calendar years 1975 and 1976, W did not exercise her right and it lapsed as to those years. In the calendar years 1977 and 1978, in which years the trust had not distributable net income, she exercised her right and withdrew \$4,000 in 1977 and \$5,000 in 1978. No accumulation distribution was made by the trust in the calendar years 1975 and 1976. An accumulation distribution of \$4,000 was made in 1977 and an accumulation distribution of \$5,000 was made in 1978. The accumulation distribution for the years 1977 and 1978 is not reduced by any amount of income of the trust attributable to her under section 678 by reason of her power of withdrawal.

[T.D. 7204, 37 FR 17137, Aug. 25, 1972]

§ 1.665(b)-2A Special rules for accumulation distributions made in taxable years beginning before January 1, 1974.

(a) *General rule.* Section 331(d)(2)(A) of the Tax Reform Act of 1969 excludes certain accumulated income from the tax imposed by section 668(a)(2) by providing certain exceptions from the definition of an "accumulation distribution." Any amount paid, credited, or required to be distributed by a trust (other than a foreign trust created by a U.S. person) during a taxable year of the trust beginning after December 31, 1968, and before January 1, 1974, shall not be subject to the tax imposed by section 668(a)(2) to the extent of the portion of such amount that (1) would be allocated under section 666(a) to a preceding taxable year of the trust beginning before January 1, 1969, and (2)

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would not have been deemed an accumulation distribution because of the provisions of paragraphs (1), (2), (3), or (4) of section 665(b) as in effect on December 31, 1968, had the trust distributed such amounts on the last day of its last taxable year beginning before January 1, 1969. However, the \$2,000 *de minimis* exception formerly in section 665(b) does not apply in the case of any distribution made in a taxable year of a trust beginning after December 31, 1968. Amounts to which this exclusion applies shall reduce the undistributed net income of the trust for the preceding taxable year or years to which such amounts would be allocated under section 666(a). However, since section 668(a)(2) does not apply to such amounts, no amount of taxes imposed on the trust allocable to such undistributed net income is deemed distributed under section 666 (b) and (c).

(b) *Application of general rule.* The rule expressed in paragraph (a) of this section is applied to the exceptions formerly in section 665(b) as follows:

(1) *Distributions from amounts accumulated while beneficiary is under 21.* (i) Paragraph (1) of section 665(b) as in effect on December 31, 1968, provided that amounts paid, credited, or required to be distributed to a beneficiary as income accumulated before the birth of such beneficiary or before such beneficiary attains the age of 21 were not to be considered to be accumulation distributions. If an accumulation distribution is made in a taxable year of the trust beginning after December 31, 1968, and before January 1, 1974, and under section 666(a) such accumulation distribution would be allocated to a preceding taxable year beginning before January 1, 1969, no tax shall be imposed under section 668(a)(2) to the extent the income earned by the trust for such preceding taxable year would be deemed under § 1.665(b)-2(b)(1) to have been accumulated before the beneficiary's birth or before his 21st birthday. The provisions of this subparagraph may be illustrated by the following example:

Example. A trust on the calendar year basis was established on January 1, 1965, to accumulate the income during the minority of B, and to pay the accumulated income over to B upon his attaining the age of 21. B's 21st

birthday is January 1, 1973. On January 2, 1973, the trustee pays over to B all the accumulated income of the trust. The distribution is an accumulation distribution that may be allocated under section 666(a) to 1968, 1969, 1970, 1971, and 1972 (the 5 preceding taxable years as defined in § 1.665(e)-1A). To the extent the distribution is allocated to 1968, no tax is imposed under section 668(a)(2).

(ii) As indicated in paragraph (a) of this section, a distribution of an amount excepted from the tax otherwise imposed under section 668(a)(2) will reduce undistributed net income for the purpose of determining the effect of a future distribution. Thus, under the facts of the example in subdivision (i) of this subparagraph, the undistributed net income for the trust's taxable year 1968 would be reduced by the amount of the distribution allocated to that year under section 666(a).

(2) *Emergency distributions.* Paragraph (2) of section 665(b) as in effect on December 31, 1968, provided an exclusion from the definition of an accumulation distribution for amounts properly paid or credited to a beneficiary to meet his emergency needs. Therefore, if an accumulation distribution is made from a trust in a taxable year beginning before January 1, 1974, and under section 666(a) such accumulation distribution would be allocated to a preceding taxable year of the trust beginning before January 1, 1969, no tax shall be imposed under section 668(a)(2) if such distribution would have been considered an emergency distribution under § 1.665(b)-2(b)(2) had it been made in a taxable year of the trust beginning before January 1, 1969. For example, assume a trust on a calendar year basis in 1972 makes an accumulation distribution which under § 1.665(b)-2(b)(2) would be considered an emergency distribution and under section 666(a) the distribution would be allocated to the years 1967, 1968, and 1969. To the extent such amount is allocated to 1967 and 1968, no tax would be imposed under section 668(a)(2).

(3) *Certain distributions at specified ages.* Paragraph (3) of section 665(b) as in effect on December 31, 1968, provided an exclusion (in the case of certain trusts created before January 1, 1954) from the definition of an accumulation distribution for amounts properly paid

or credited to a beneficiary upon his attaining a specified age or ages, subject to certain restrictions (see § 1.665(b)-2(b)(3)). Therefore, a distribution from a trust in a taxable year beginning after December 31, 1968, will not be subject to the tax imposed under section 668(a)(2) to the extent such distribution would be allocated to a preceding taxable year of the trust beginning before January 1, 1969, if such distribution would have qualified under the provisions of § 1.665(b)-2(b)(3) had it been made in a taxable year of the trust to which such section was applicable.

(4) *Certain final distributions.* Paragraph (4) of section 665(b) as in effect on December 31, 1968, provided an exclusion from the definition of an accumulation distribution for amounts properly paid or credited to a beneficiary as a final distribution of the trust if such final distribution was made more than 9 years after the date of the last transfer to such trust. Therefore, amounts properly paid or credited to a beneficiary as a final distribution of a trust in a taxable year of a trust beginning after December 31, 1968, and before January 1, 1974, will not be subject to the tax imposed under section 668(a)(2) to the extent such distribution would be allocated to a preceding taxable year of the trust beginning before January 1, 1969, if such final distribution was made more than 9 years after the date of the last transfer to such trust. The provisions of this subparagraph may be illustrated by the following example:

Example. A trust on a calendar year basis was established on January 1, 1958, and no additional transfers were made to it. On January 1, 1973, the trustee terminates the trust and on the same day he makes a final distribution to the beneficiary, B. The distribution is an accumulation distribution that may be allocated under section 666(a) to 1968, 1969, 1970, 1971, and 1972 (the 5 preceding taxable years as defined in § 1.665(e)-1A). Because more than 9 years elapsed between the date of the last transfer to the trust and the date of final distribution, the distribution is not taxed under section 668 (a) (2) to the extent it would be allocated to 1968 under section 666(a).

[T.D. 7204, 37 FR 17138, Aug. 25, 1972]

§ 1.665(c)-1A Special rule applicable to distributions by certain foreign trusts.

(a) *In general.* Except as provided in paragraph (b) of this section, for purposes of section 665 any amount paid to a U.S. person which is from a payor who is not a U.S. person and which is derived directly or indirectly from a foreign trust created by a U.S. person shall be deemed in the year of payment to the U.S. person to have been directly paid to the U.S. person by the trust. For example, if a nonresident alien receives a distribution from a foreign trust created by a U.S. person and then pays the amount of the distribution over to a U.S. person, the payment of such amount to the U.S. person represents an accumulation distribution to the U.S. person from the trust to the extent that the amount received would have been an accumulation distribution had the trust paid the amount directly to the U.S. person in the year in which the payment was received by the U.S. person. This section also applies in a case where a nonresident alien receives indirectly an accumulation distribution from a foreign trust created by a U.S. person and then pays it over to a U.S. person. An example of such a transaction is one where the foreign trust created by a U.S. person makes the distribution to an intervening foreign trust created by either a U.S. person or a person other than a U.S. person and the intervening trust distributes the amount received to a nonresident alien who in turn pays it over to a U.S. person. Under these circumstances, it is deemed that the payment received by the U.S. person was received directly from a foreign trust created by a U.S. person.

(b) *Limitation.* In the case of a distribution to a beneficiary who is a U.S. person, paragraph (a) of this section does not apply if the distribution is received by such beneficiary under circumstances indicating lack of intent on the part of the parties to circumvent the purposes for which section 7 of the Revenue Act of 1962 (76 Stat. 985) was enacted.

[T.D. 7204, 37 FR 17139 Aug. 25, 1972]