

**§ 1.665(e)-1A**

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means the amount of Federal income taxes for the taxable year properly attributable to that portion of the excess of capital gains over capital losses of the trust that is allocable to corpus for such taxable year. Such amount is the total of:

(i) The amount computed under subparagraph (2) of this paragraph (the minimum tax), plus

(ii) The amount that bears the same relationship to the total taxes of the trust for the year (other than the minimum tax), computed after the allowance of credits under section 642(a), as (a) the excess of capital gains over capital losses for such year that are not included in distributable net income, computed after its share of the deduction under section 1202 (relating to the deduction for capital gains) has been taken into account, bears to the greater of (b) the total taxable income of the trust for such year, or (c) the amount of capital gains computed under (a) of this subdivision.

However, if the alternative tax computation under section 1201(b) is used and there are no net short-term gains, the amount is the amount of the alternative tax imposed on the trust and attributable to the capital gain. The application of this subparagraph may be illustrated by the following example, which assumes that the alternative tax computation is not used:

*Example.* Assume the same facts as in the example in paragraph (b)(1). The capital gains not included in d.n.i. are \$10,000, and the deduction under section 1202 is \$5,000. The amount of taxes imposed on the trust attributable to undistributed capital gain is \$1,468, computed as follows:

\$3,787 (total taxes) × \$5,000 (capital gains not included in d.n.i. less section 1202 deductions)	
divided by \$12,900 (taxable income) .....	\$1,468

(2) *Minimum tax.* The term *taxes imposed on the trust attributable to the undistributed capital gain* also includes the minimum tax for tax preferences imposed on the trust by section 56 with respect to the undistributed capital gain. The amount of such minimum tax so included bears the same relation to the total amount of minimum tax imposed on the trust by section 56 for the taxable year as one-half the net capital gain (net section 1201 gain for taxable years beginning before January 1, 1977)

(as defined in section 1222(11)) from such taxable year bears to the sum of the items of tax preference of the trust for such taxable year which are apportioned to the trust in accordance with § 1.58-3(a) (1).

(3) *Reduction for prior distribution.* If in any taxable year a capital gain distribution is made by the trust which results in a throwback to a prior year, the taxes of the prior year imposed on the trust attributable to any remaining undistributed capital gain of the prior year are the taxes prescribed in subparagraph (1) of this paragraph reduced by the taxes of the prior year deemed distributed under section 669 (d) or (e). The provisions of this subparagraph may be illustrated by the following example:

*Example.* Assume the same facts as in the example in subparagraph (1) of this paragraph. In 1976, the trust makes a capital gain distribution, of which an amount of undistributed capital gain is deemed distributed in 1974. Taxes imposed on the trust (in the amount of \$500) attributable to the undistributed capital gain are therefore deemed distributed in such year. Consequently, the taxes imposed on the trust attributable to the remaining undistributed capital gain are \$968 (\$1,468 less \$500).

[T.D. 7204, 37 FR 17139, Aug. 25, 1972, as amended by T.D. 7728, 45 FR 72650, Nov. 3, 1980]

**§ 1.665(e)-1A Preceding taxable year.**

(a) *Definition*—(1) *Domestic trusts*—(i) *In general.* For purposes of subpart D, in the case of a trust other than a foreign trust created by a U.S. person, the term *preceding taxable year* serves to identify and limit the taxable years of a trust to which an accumulation distribution consisting of undistributed net income or undistributed capital gain may be allocated (or “thrown back”) under section 666(a) and 669(a). An accumulation distribution consisting of undistributed net income or undistributed capital gain may not be allocated or “thrown back” to a taxable year of a trust if such year is not a “preceding taxable year.”

(ii) *Accumulation distributions.* In the case of an accumulation distribution consisting of undistributed net income made in a taxable year beginning before January 1, 1974, any taxable year of the trust that precedes by more than

5 years the taxable year of the trust in which such accumulation distribution was made is not a "preceding taxable year." Thus, for a domestic trust on a calendar year basis, calendar year 1967 is not a "preceding taxable year" with respect to an accumulation distribution made in calendar year 1973, whereas calendar year 1968 is a "preceding taxable year." In the case of an accumulation distribution made during a taxable year beginning after December 31, 1973, any taxable year of the trust that begins before January 1, 1969, is not a "preceding taxable year." Thus, for a domestic trust on a calendar year basis, calendar year 1968 is not a "preceding taxable year" with respect to an accumulation distribution made in calendar year 1975, whereas calendar year 1969 is a "preceding taxable year."

(iii) *Capital gain distributions.* In the case of an accumulation distribution that is a capital gain distribution, any taxable year of the trust that (a) begins before January 1, 1969, or (b) is prior to the first year in which income is accumulated, whichever occurs later, is not a "preceding taxable year." Thus, for the purpose of capital gain distributions and section 669, only taxable years beginning after December 31, 1968, can be "preceding taxable years." See § 1.688(a)-1A(c).

(2) *Foreign trusts created by U.S. persons.* For purposes of subpart D, in the case of a foreign trust created by a U.S. person, the term "preceding taxable year" does not include any taxable year to which part I of subchapter J does not apply. See section 683 and regulations thereunder. Accordingly, the provisions of subpart D may not, in the case of a foreign trust created by a U.S. person, be applied to any taxable year which begins before 1954 or ends before August 17, 1954. For example, if a foreign trust created by a U.S. person (reporting on the calendar year basis) makes a distribution during the calendar year 1970 of income accumulated during prior years, the earliest year of the trust to which the accumulation distribution may be allocated under such subpart D is 1954, but it may not be allocated to 1953 and prior years, since the Internal Revenue Code of 1939 applies to those years.

(b) *Simple trusts.* A taxable year of a trust during which the trust was a simple trust (that is, was subject to subpart B) for the entire year shall not be considered a "preceding taxable year" unless during such year the trust received "outside income" or unless the trustee did not distribute all of the income of the trust that was required to be distributed currently for such year. In such event, undistributed net income for such year shall not exceed the greater of the "outside income" or income not distributed during such year. For purposes of this paragraph, the term *outside income* means amounts that are included in distributable net income of the trust for the year but that are not "income" of the trust as that term is defined in § 1.643(b)-1. Some examples of "outside income" are:

- (1) Income taxable to the trust under section 691;
- (2) Unrealized accounts receivable that were assigned to the trust; and
- (3) Distributions from another trust that include distributable net income or undistributed net income of such other trust.

The term *outside income*, however, does not include amounts received as distributions from an estate, other than income specified in (1) and (2), for which the estate was allowed a deduction under section 661(a). The application of this paragraph may be illustrated by the following examples:

*Example 1.* By his will D creates a trust for his widow W. The terms of the trust require that the income be distributed currently (i.e., it is a simple trust), and authorize the trustee to make discretionary payments of corpus to W. Upon W's death the trust corpus is to be distributed to D's then living issue. The executor of D's will makes a \$10,000 distribution of corpus to the trust that carries out estate income consisting of dividends and interest to the trust under section 662(a)(2). The trust reports this income as its only income on its income tax return for its taxable year in which ends the taxable year of the estate in which the \$10,000 distribution was made, and pays a tax thereon of \$2,106. Thus, the trust has undistributed net income of \$7,894 (\$10,000 - \$2,106). Several years later the trustee makes a discretionary corpus payment of \$15,000 to W. This payment is an accumulation distribution under section

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665(b). However, since the trust had no “outside income” in the year of the estate distribution, such year is not a preceding taxable year. Thus, W is not treated as receiving undistributed net income of \$7,894 and taxes thereon of \$2,106 for the purpose of including the same in her gross income under section 668. The result would be the same if the invasion power were not exercised and the accumulation distribution occurred as a result of the distribution of the corpus to D’s issue upon the death of W.

*Example 2.* Trust A, a simple trust on the calendar year basis, received in 1972 extraordinary dividends or taxable stock dividends that the trustee in good faith allocated to corpus, but that are determined in 1974 to have been currently distributable to the beneficiary. See section 643(a)(4) and § 1.643(a)-4. Trust A would qualify for treatment under subpart C for 1974, the year of distribution of the extraordinary dividends or taxable stock dividends, because the distribution is not out of income of the current taxable year and is treated as another amount properly paid or credited or required to be distributed for such taxable year within the meaning of section 661(a) (2). Also, the distribution in 1974 qualifies as an accumulation distribution for the purposes of subpart D. For purposes only of such subpart D, trust A would be treated as subject to the provisions of such subpart C for 1972, the preceding taxable year in which the extraordinary or taxable stock dividends were received, and, in computing undistributed net income for 1972, the extraordinary or taxable stock dividends would be included in distributable net income under section 643(a). The rule stated in the preceding sentence would also apply if the distribution in 1974 was made out of corpus without regard to a determination that the extraordinary dividends or taxable stock dividends in question were currently distributable to the beneficiary.

[T.D. 7204, 37 FR 17141, Aug. 25, 1972]

**§ 1.665(f)-1A Undistributed capital gain.**

(a) *Domestic trusts.* (1) The term *undistributed capital gain* means (in the case of a trust other than a foreign trust created by a U.S. person), for any taxable year of the trust beginning after December 31, 1968, the gains in excess of losses for that year from the sale or exchange of capital assets of the trust less:

- (i) The amount of such gains that are included in distributable net income under section 643(a)(3) and § 1.643(a)-3.
- (ii) The amount of taxes imposed on the trust for such year attributable to

such gains, as defined in § 1.665(d)-1A, and

(iii) In the case of a trust that does not use the alternative method for computing taxes on capital gains of the taxable year, the excess of deductions (other than deductions allowed under section 642(b) relating to personal exemption or section 642(c) relating to charitable contributions) over distributable net income for such year to the extent such excess deductions are properly allowable in determining taxable income for such year.

For purposes of computing the amount of capital gain under this paragraph, no deduction under section 1202, relating to deduction for excess of capital gains over capital losses, shall be taken into account. The application of this subparagraph may be illustrated by the following example:

*Example.* Under the terms of the trust, the trustee must distribute all income currently and has discretion to distribute capital gain to A or to allocate it to corpus. During the taxable year 1971 the trust recognized capital gain in the amount of \$15,000, and capital losses of \$5,000, and had interest income (after expenses) of \$6,000. The trustee distributed \$8,000 to A, consisting of \$6,000 of interest and \$2,000 of capital gain. The \$2,000 of gain distributed to A is included in the computation of distributable net income under § 1.643(a)-3. The balance of the capital gain is not included in distributable net income since it is allocated to corpus and not paid, credited, or required to be distributed to any beneficiary. The trust paid taxes of \$671, all of which are attributable under § 1.665(d)-1A to the undistributed capital gain. The amount of undistributed capital gain of the trust for 1971 is therefore \$7,329, computed as follows:

Total capital gains .....	\$15,000
Less: Capital losses .....	5,000
Gains in excess of losses .....	<u>10,000</u>
Less:	
Amount of capital gain included in distributable net income .....	2,000
Taxes imposed on the trust attributable to the undistributed capital gain (see § 1.665(d)-1A) .....	671
	<u>2,671</u>
Undistributed capital gain .....	<u>7,329</u>

(2) For purposes of subparagraph (1) of this paragraph, the term *losses for that year* includes losses of the trusts