

§ 1.661(c)-2

section 116, items of distributable net income which are not included in the gross income of the estate or trust.

[T.D. 6777, 29 FR 17809, Dec. 16, 1964]

§ 1.661(c)-2 Illustration of the provisions of section 661.

The provisions of section 661 may be illustrated by the following example:

Example. (a) Under the terms of a trust, which reports on the calendar year basis, \$10,000 a year is required to be paid out of income to a designated charity. The balance of the income may, in the trustee's discretion, be accumulated or distributed to beneficiary A. Expenses are allocable against income and the trust instrument requires a reserve for depreciation. During the taxable year 1955 the trustee contributes \$10,000 to charity and in his discretion distributes \$15,000 of income to A. The trust has the following items of income and expense for the taxable year 1955:

Partially tax-exempt interest.....	10,000
Fully tax-exempt interest.....	10,000
Rents.....	20,000
Rental expenses.....	2,000
Depreciation of rental property.....	3,000
Trustee's commissions.....	5,000

(b) The income of the trust for fiduciary accounting purposes is \$40,000, computed as follows:

Dividends.....	\$10,000
Partially tax-exempt interest.....	10,000
Fully tax-exempt interest.....	10,000
Rents.....	20,000
Total.....	50,000
Less:	
Rental expenses.....	\$2,000
Depreciation.....	3,000
Trustee's commissions.....	5,000
	10,000

Income as computed under section 643(b)..... 40,000

(c) The distributable net income of the trust as computed under section 643(a) is \$30,000, determined as follows:

Rents.....		\$20,000
Dividends.....		10,000
Partially tax-exempt interest.....		10,000
Fully tax-exempt interest.....	\$10,000	
Less:		
Expenses allocable thereto (10,000/50,000×\$5,000).....	\$1,000	
Charitable contributions allocable thereto (10,000/50,000×\$10,000).....	2,000	
	3,000	
		7,000
Total.....		47,000
Deductions:		
Rental expenses.....	2,000	
Depreciation of rental property.....	3,000	
Trustee's commissions (\$5,000 less \$1,000 allocated to tax-exempt interest).....	4,000	
Charitable contributions (\$10,000 less \$2,000 allocated to tax-exempt interest) ..	8,000	
	17,000	
Distributable net income (section 643(a)).....		30,000

(d) The character of the amounts distributed under section 661(a), determined in accordance with the rules prescribed in §§ 1.661(b)-1 and 1.661(b)-2 is shown by the following table (for the purpose of this alloca-

tion, it is assumed that the trustee elected to allocate the trustee's commissions to rental income except for the amount required to be allocated to tax-exempt interest):

	Rental income	Taxable dividends	Excluded dividends	Partially tax-exempt interest	Tax-exempt interest	Total
Trust income	\$20,000	\$9,950	\$50	\$10,000	\$10,000	\$50,000
Less:						
Charitable contributions	4,000	2,000	.....	2,000	2,000	10,000
Rental expenses	2,000	.....	.....	.....	.....	2,000
Depreciation	3,000	.....	.....	.....	.....	3,000

	Rental income	Taxable dividends	Excluded dividends	Partially tax-exempt interest	Tax-exempt interest	Total
Trustee's commissions	4,000	.....	.....	.....	1,000	5,000
Total deductions	13,000	2,000	0	2,000	3,000	20,000
Distributable net income	7,000	7,950	50	8,000	7,000	30,000
Amounts deemed distributed under section 661(a) before applying the limitation of section 661(c)	3,500	3,975	25	4,000	3,500	15,000

In the absence of specific provisions in the trust instrument for the allocation of different classes of income, the charitable contribution is deemed to consist of a pro rata portion of the gross amount of each item of income of the trust (except dividends excluded under section 116) and the trust is deemed to have distributed to A a pro rata portion (one-half) of each item of income included in distributable net income.

(e) The taxable income of the trust is \$11,375 computed as follows:

Rental income	\$20,000
Dividends (\$10,000 less \$50 exclusion)	9,950
Partially tax-exempt interest	10,000
Gross income	39,950
Deductions:	
Rental expenses	\$2,000
Depreciation of rental property ...	3,000
Trustee's commissions	4,000
Charitable contributions	8,000
Distributions to A	11,475
Personal exemption	100
	28,575
Taxable income	11,375

In computing the taxable income of the trust no deduction is allowable for the portions of the charitable contributions deduction (\$2,000) and trustee's commissions (\$1,000) which are treated under section 661(b) as attributable to the tax-exempt interest excludable from gross income. Also, of the dividends of \$4,000 deemed to have been distributed to A under section 661(a), \$25 (25/50ths of \$50) is deemed to have been distributed from the excluded dividends and is not an allowable deduction to the trust. Accordingly, the deduction allowable under section 661 is deemed to be composed of \$3,500 rental income, \$3,975 of dividends, and \$4,000 partially tax-exempt interest. No deduction is allow-

able for the portion of tax-exempt interest or for the portion of the excluded dividends deemed to have been distributed to the beneficiary.

(f) The trust is entitled to the credit allowed by section 34 with respect to dividends of \$5,975 (\$9,950 less \$3,975 distributed to A) included in gross income. Also, the trust is allowed the credit provided by section 35 with respect to partially tax-exempt interest of \$6,000 (\$10,000 less \$4,000 deemed distributed to A) included in gross income.

(g) Dividends of \$4,000 allocable to A are to be aggregated with his other dividends (if any) for purposes of the dividend exclusion under section 116 and the dividend received credit under section 84.

§ 1.662(a)-1 Inclusion of amounts in gross income of beneficiaries of estates and complex trusts; general.

There is included in the gross income of a beneficiary of an estate or complex trust the sum of:

(a) Amounts of income required to be distributed currently to him, and

(b) All other amounts properly paid, credited, or required to be distributed to him

by the estate or trust. The preceding sentence is subject to the rules contained in § 1.662(a)-2 (relating to currently distributable income), § 1.662(a)-3 (relating to other amounts distributed), and §§ 1.662(b)-1 and 1.662(b)-2 (relating to character of amounts). Section 662 has no application to amounts excluded under section 663(a).