

transfer is eligible for the fair market value exception of paragraph (a)(4) of this section.

Example 6. Effect of subsequent obligation on original obligation. A transfers property that has a fair market value of 1000X to FT in exchange for an obligation that satisfies the requirements of paragraph (d)(1) of this section. A is a related person (as defined in §1.679-1(c)(5)) with respect to FT. Two years later, A transfers an additional 2000X to FT and receives another obligation from FT that has a maturity date four years from the date that the second obligation was issued. Under paragraph (d)(2) of this section, the original obligation is deemed to have the maturity date of the second obligation. Under paragraph (a) of this section, A is treated as having made a transfer in an amount equal to the original obligation's adjusted issue price (within the meaning of §1.1275-1(b)) plus any accrued but unpaid qualified stated interest (within the meaning of §1.1273-1(c)) as of the date of issuance of the second obligation. The second obligation is tested separately to determine whether it is a qualified obligation for purposes of applying paragraph (a) of this section to the second transfer.

[T.D. 8955, 66 FR 37889, July 20, 2001]

§ 1.679-5 Pre-immigration trusts.

(a) *In general.* If a nonresident alien individual becomes a U.S. person and the individual has a residency starting date (as determined under section 7701(b)(2)(A)) within 5 years after directly or indirectly transferring property to a foreign trust (the original transfer), the individual is treated as having transferred to the trust on the residency starting date an amount equal to the portion of the trust attributable to the property transferred by the individual in the original transfer.

(b) *Special rules—(1) Change in grantor trust status.* For purposes of paragraph (a) of this section, if a nonresident alien individual who is treated as owning any portion of a trust under the provisions of subpart E of part I of subchapter J, chapter 1 of the Internal Revenue Code, subsequently ceases to be so treated, the individual is treated as having made the original transfer to the foreign trust immediately before the trust ceases to be treated as owned by the individual.

(2) *Treatment of undistributed income.* For purposes of paragraph (a) of this section, the property deemed transferred to the foreign trust on the residency starting date includes undistributed net income, as defined in section

665(a), attributable to the property deemed transferred. Undistributed net income for periods before the individual's residency starting date is taken into account only for purposes of determining the amount of the property deemed transferred.

(c) *Examples.* The rules of this section are illustrated by the following examples:

Example 1. Nonresident alien becomes resident alien. On January 1, 2002, A, a nonresident alien individual, transfers property to a foreign trust, FT. On January 1, 2006, A becomes a resident of the United States within the meaning of section 7701(b)(1)(A) and has a residency starting date of January 1, 2006, within the meaning of section 7701(b)(2)(A). Under paragraph (a) of this section, A is treated as a U.S. transferor and is deemed to transfer the property to FT on January 1, 2006. Under paragraph (b)(2) of this section, the property deemed transferred to FT on January 1, 2006, includes the undistributed net income of the trust, as defined in section 665(a), attributable to the property originally transferred.

Example 2. Nonresident alien loses power to re-vest property. On January 1, 2002, A, a nonresident alien individual, transfers property to a foreign trust, FT. A has the power to re-vest absolutely in himself the title to such property transferred and is treated as the owner of the trust pursuant to sections 676 and 672(f). On January 1, 2008, the terms of FT are amended to remove A's power to re-vest in himself title to the property transferred, and A ceases to be treated as the owner of FT. On January 1, 2010, A becomes a resident of the United States. Under paragraph (b)(1) of this section, for purposes of paragraph (a) of this section A is treated as having originally transferred the property to FT on January 1, 2008. Because this date is within five years of A's residency starting date, A is deemed to have made a transfer to the foreign trust on January 1, 2010, his residency starting date. Under paragraph (b)(2) of this section, the property deemed transferred to the foreign trust on January 1, 2010, includes the undistributed net income of the trust, as defined in section 665(a), attributable to the property deemed transferred.

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§ 1.679-6 Outbound migrations of domestic trusts.

(a) *In general.* Subject to the provisions of paragraph (b) of this section, if an individual who is a U.S. person transfers property to a trust that is not a foreign trust, and such trust becomes a foreign trust while the U.S. person is

§ 1.679-7

26 CFR Ch. I (4-1-02 Edition)

alive, the U.S. individual is treated as a U.S. transferor and is deemed to transfer the property to a foreign trust on the date the domestic trust becomes a foreign trust.

(b) *Amount deemed transferred.* For purposes of paragraph (a) of this section, the property deemed transferred to the trust when it becomes a foreign trust includes undistributed net income, as defined in section 665(a), attributable to the property previously transferred. Undistributed net income for periods prior to the migration is taken into account only for purposes of determining the portion of the trust that is attributable to the property transferred by the U.S. person.

(c) *Example.* The following example illustrates the rules of this section. For purposes of the example, *A* is a resident alien, *B* is *A*'s son, who is a resident alien, and *DT* is a domestic trust. The example is as follows:

Example. Outbound migration of domestic trust. On January 1, 2002, *A* transfers property to *DT*, for the benefit of *B*. On January 1, 2003, *DT* acquires a foreign trustee who has the power to determine whether and when distributions will be made to *B*. Under section 7701(a)(30)(E) and § 301.7701-7(d)(ii)(A) of this chapter, *DT* becomes a foreign trust on January 1, 2003. Under paragraph (a) of this section, *A* is treated as transferring property to a foreign trust on January 1, 2003. Under paragraph (b) of this section, the property deemed transferred to the trust when it becomes a foreign trust includes undistributed net income, as defined in section 665(a), attributable to the property deemed transferred.

[T.D. 8955, 66 FR 37889, July 20, 2001]

§ 1.679-7 Effective dates.

(a) *In general.* Except as provided in paragraph (b) of this section, the rules of §§ 1.679-1, 1.679-2, 1.679-3, and 1.679-4 apply with respect to transfers after August 7, 2000.

(b) *Special rules.* (1) The rules of § 1.679-4(c) and (d) apply to an obligation issued after February 6, 1995, whether or not in accordance with a pre-existing arrangement or understanding. For purposes of the rules of § 1.679-4(c) and (d), if an obligation issued on or before February 6, 1995, is modified after that date, and the modification is a significant modification within the meaning of § 1.1001-3, the ob-

ligation is treated as if it were issued on the date of the modification. However, the penalty provided in section 6677 applies only to a failure to report transfers in exchange for obligations issued after August 20, 1996.

(2) The rules of § 1.679-5 apply to persons whose residency starting date is after August 7, 2000.

(3) The rules of § 1.679-6 apply to trusts that become foreign trusts after August 7, 2000.

[T.D. 8955, 66 FR 37889, July 20, 2001]

MISCELLANEOUS

§ 1.681(a)-1 Limitation on charitable contributions deductions of trusts; scope of section 681.

Under section 681, the unlimited charitable contributions deduction otherwise allowable to a trust under section 642(c) is, in general, subject to percentage limitations, corresponding to those applicable to contributions by an individual under section 170(b)(1) (A) and (B), under the following circumstances:

(a) To the extent that the deduction is allocable to "unrelated business income";

(b) For taxable years beginning before January 1, 1970, if the trust has engaged in a prohibited transaction;

(c) For taxable years beginning before January 1, 1970, if income is accumulated for a charitable purpose and the accumulation is (1) unreasonable, (2) substantially diverted to a non-charitable purpose, or (3) invested against the interests of the charitable beneficiaries.

Further, if the circumstance set forth in paragraph (a) or (c) of this section is applicable, the deduction is limited to income actually paid out for charitable purposes, and is not allowed for income only set aside or to be used for those purposes. If the circumstance set forth in paragraph (b) of this section is applicable, deductions for contributions to the trust may be disallowed. The provisions of section 681 are discussed in detail in §§ 1.681(a)-2 through 1.681(c)-1. For definition of the term "income", see section 643(b) and § 1.643(b)-1.

[T.D. 6500, 25 FR 11814, Nov. 26, 1960, as amended by T.D. 7428, 41 FR 34627, Aug. 16, 1976]