relating to tax-exempt interest, foreign income, and excluded dividends. For example: Assume that the distributable net income of a trust as computed under section 643(a) amounts to $99,000 but includes nontaxable income of $9,000. Then distributable net income for the purpose of determining the deduction allowable under section 651 is $90,000 ($99,000 less $9,000 nontaxable income).

§ 1.652(a)–1 Simple trusts; inclusion of amounts in income of beneficiaries.

Subject to the rules in §§1.652(a)–2 and 1.652(b)–1, a beneficiary of a simple trust includes in his gross income for the taxable year the amounts of income required to be distributed to him for such year, whether or not distributed. Thus, the income of a simple trust is includible in the beneficiary’s gross income for the taxable year in which the income is required to be distributed currently even though, as a matter of practical necessity, the income is not distributed until after the close of the taxable year of the trust. See §1.642(a)(3)–2 with respect to time of receipt of dividends. See §1.652(c)–1 for treatment of amounts required to be distributed where a beneficiary and the trust have different taxable years. The term income required to be distributed currently includes income required to be distributed currently which is in 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 $90,000, A will receive $60,000 and B $30,000. 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 includible 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 qualified 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(a)(2). 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.