

Taxation on the Accumulated Income of Trusts

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Under the present law, the income which is accumulated in the trust and is not distributed to the beneficiaries when it is acquired should be taxed as the income of either the beneficiary or the grantor. But in some cases, in which, for example, the grantor has neither control of nor benefit from the trust property, the taxation to the grantor would not be reasonable, needless to say taxation to his legal heirs on his death. On the other hand the tax on the beneficiary might be seemed troublesome from the view point of the flexibility of trusts because he actually gets nothing to pay tax with it.

Considering these problems it seems necessary to reform our tax system concerning trust accumulations. There could be three alternatives here.

1) the 'throwback rule' method

Adopting so called "throwback rule", which had been adopted originally by the United States federal income taxation in 1954 and was virtually abandoned in 1997, might be one of the strongest answer to our problem. But the history of this rule in the United States shows us that satisfactory compromise between the correctness of the calculation of the amount of tax and the administrative feasibility of both trustee-taxpayer and the tax administration, can hardly be reached under this method.

2) the flat rate separate taxation

The separate tax on the accumulated income to the trust property with the flat rate, accompanied with the exempted distribution to the

beneficiary, would be also good alternative. However, there would be some over-taxation or under-taxation according to the difference between the actual tax rate of the beneficiary and of the trust, the latter might be the same rate with the highest rate of the individual income tax. Therefore the reasonableness of this method depends on the degree of the progressiveness of the individual tax rate.

3) the 'interest tax' method

The interest tax on the accumulated income while it is reserved could also be considered one of the good solutions. Under this system the accumulated income would be taxed as a part of the beneficiary when it is actually distributed. Although some technical refinement is necessary, this method would enable to give the flexibility to the trust as well as to reach the reasonable equity of tax.