

1 H.327

2 Introduced by Representative Koch of Barre Town

3 Referred to Committee on

4 Date:

5 Subject: Decedents' estates; uniform principal and income act

6 Statement of purpose: This bill proposes to enact an updated version of the
7 uniform principal and income act.

8 An act relating to the uniform principal and income act

9 It is hereby enacted by the General Assembly of the State of Vermont:

10 Sec. 1. 14 V.S.A. chapter 118 is added to read:

11 CHAPTER 118. UNIFORM PRINCIPAL AND INCOME ACT

12 Subchapter 1. General Provisions

13 § 3321. SHORT TITLE

14 This Act may be cited as the Uniform Principal and Income Act.

15 § 3322. DEFINITIONS

16 As used in this chapter:

17 (1) "Accounting period" means a calendar year unless another 12-month
18 period is selected by a fiduciary. The term includes a portion of a calendar
19 year or other 12-month period that begins when an income interest begins or
20 ends when an income interest ends.

1 (2) “Beneficiary” includes, in the case of a decedent’s estate, an heir,
2 legatee, and devisee and, in the case of a trust, an income beneficiary and a
3 remainder beneficiary.

4 (3) “Fiduciary” means a personal representative or a trustee. The term
5 includes an executor, administrator, successor personal representative, special
6 administrator, and a person performing substantially the same function.

7 (4) “Income” means money or property that a fiduciary receives as
8 current return from a principal asset. The term includes a portion of receipts
9 from a sale, exchange, or liquidation of a principal asset, to the extent provided
10 in subchapter 4 of this chapter.

11 (5) “Income beneficiary” means a person to whom net income of a trust
12 is or may be payable.

13 (6) “Income interest” means the right of an income beneficiary to
14 receive all or part of net income, whether the terms of the trust require it to be
15 distributed or authorize it to be distributed in the trustee’s discretion.

16 (7) “Mandatory income interest” means the right of an income
17 beneficiary to receive net income that the terms of the trust require the
18 fiduciary to distribute.

19 (8) “Net income” means the total receipts allocated to income during an
20 accounting period minus the disbursements made from income during the

1 period, plus or minus transfers under this chapter to or from income during the
2 period.

3 (9) "Person" means an individual, corporation, business trust, estate,
4 trust, partnership, limited liability company, association, joint venture,
5 government; governmental subdivision, agency, or instrumentality; public
6 corporation, or any other legal or commercial entity.

7 (10) "Principal" means property held in trust for distribution to a
8 remainder beneficiary when the trust terminates.

9 (11) "Remainder beneficiary" means a person entitled to receive
10 principal when an income interest ends.

11 (12) "Terms of a trust" means the manifestation of the intent of a settlor
12 or decedent with respect to the trust, expressed in a manner that admits of its
13 proof in a judicial proceeding, whether by written or spoken words or by
14 conduct.

15 (13) "Trustee" includes an original, additional, or successor trustee,
16 whether or not appointed or confirmed by a court.

17 § 3323. FIDUCIARY DUTIES; GENERAL PRINCIPLES

18 (a) In allocating receipts and disbursements to or between principal and
19 income, and with respect to any matter within the scope of subchapter 2 or 3 of
20 this chapter, a fiduciary:

1 (1) shall administer a trust or estate in accordance with the terms of the
2 trust or the will, even if there is a different provision in this chapter;

3 (2) may administer a trust or estate by the exercise of a discretionary
4 power of administration given to the fiduciary by the terms of the trust or the
5 will, even if the exercise of the power produces a result different from a result
6 required or permitted by this chapter;

7 (3) shall administer a trust or estate in accordance with this chapter if the
8 terms of the trust or the will do not contain a different provision or do not give
9 the fiduciary a discretionary power of administration; and

10 (4) shall add a receipt or charge a disbursement to principal to the extent
11 that the terms of the trust and this chapter do not provide a rule for allocating
12 the receipt or disbursement to or between principal and income.

13 (b) In exercising the power to adjust under subsection 3324(a) of this
14 section or a discretionary power of administration regarding a matter within the
15 scope of this chapter, whether granted by the terms of a trust, a will, or this
16 chapter, a fiduciary shall administer a trust or estate impartially, based on what
17 is fair and reasonable to all of the beneficiaries, except to the extent that the
18 terms of the trust or the will clearly manifest an intention that the fiduciary
19 shall or may favor one or more of the beneficiaries. A determination in
20 accordance with this chapter is presumed to be fair and reasonable to all of the
21 beneficiaries.

1 § 3324. TRUSTEE'S POWER TO ADJUST

2 (a) A trustee may adjust between principal and income to the extent the
3 trustee considers necessary if the trustee invests and manages trust assets as a
4 prudent investor, the terms of the trust describe the amount that may or must be
5 distributed to a beneficiary by referring to the trust's income, and the trustee
6 determines, after applying the rules in subsection 3323(a) of this title, that the
7 trustee is unable to comply with subsection 3323(b) of this title.

8 (b) In deciding whether and to what extent to exercise the power conferred
9 by subsection (a) of this section, a trustee shall consider all factors relevant to
10 the trust and its beneficiaries, including the following factors to the extent they
11 are relevant:

12 (1) the nature, purpose, and expected duration of the trust;

13 (2) the intent of the settlor;

14 (3) the identity and circumstances of the beneficiaries;

15 (4) the needs for liquidity, regularity of income, and preservation and
16 appreciation of capital;

17 (5) the assets held in the trust; the extent to which they consist of
18 financial assets, interests in closely held enterprises, tangible and intangible
19 personal property, or real property; the extent to which an asset is used by a
20 beneficiary; and whether an asset was purchased by the trustee or received
21 from the settlor;

1 (6) the net amount allocated to income under the other sections of this
2 chapter and the increase or decrease in the value of the principal assets, which
3 the trustee may estimate as to assets for which market values are not readily
4 available;

5 (7) whether and to what extent the terms of the trust give the trustee the
6 power to invade principal or accumulate income or prohibit the trustee from
7 invading principal or accumulating income, and the extent to which the trustee
8 has exercised a power from time to time to invade principal or accumulate
9 income;

10 (8) the actual and anticipated effect of economic conditions on principal
11 and income and effects of inflation and deflation; and

12 (9) the anticipated tax consequences of an adjustment.

13 (c) A trustee may not make an adjustment:

14 (1) that diminishes the income interest in a trust that requires all of the
15 income to be paid at least annually to a spouse and for which an estate tax or
16 gift tax marital deduction would be allowed, in whole or in part, if the trustee
17 did not have the power to make the adjustment;

18 (2) that reduces the actuarial value of the income interest in a trust to
19 which a person transfers property with the intent to qualify for a gift tax
20 exclusion;

1 (3) that changes the amount payable to a beneficiary as a fixed annuity
2 or a fixed fraction of the value of the trust assets;

3 (4) from any amount that is permanently set aside for charitable
4 purposes under a will or the terms of a trust unless both income and principal
5 are so set aside;

6 (5) if possessing or exercising the power to make an adjustment causes
7 an individual to be treated as the owner of all or part of the trust for income tax
8 purposes, and the individual would not be treated as the owner if the trustee did
9 not possess the power to make an adjustment;

10 (6) if possessing or exercising the power to make an adjustment causes
11 all or part of the trust assets to be included for estate tax purposes in the estate
12 of an individual who has the power to remove a trustee or appoint a trustee, or
13 both, and the assets would not be included in the estate of the individual if the
14 trustee did not possess the power to make an adjustment;

15 (7) if the trustee is a beneficiary of the trust; or

16 (8) if the trustee is not a beneficiary, but the adjustment would benefit
17 the trustee directly or indirectly.

18 (d) If subdivision (c)(5), (6), (7), or (8) of this section applies to a trustee
19 and there is more than one trustee, a cotrustee to whom the provision does not
20 apply may make the adjustment unless the exercise of the power by the
21 remaining trustee or trustees is not permitted by the terms of the trust.

1 (e) A trustee may release the entire power conferred by subsection (a) of
2 this section or may release only the power to adjust from income to principal
3 or the power to adjust from principal to income if the trustee is uncertain about
4 whether possessing or exercising the power will cause one of the results
5 described in subdivisions (c)(1)–(6) or (c)(8) of this section or if the trustee
6 determines that possessing or exercising the power will or may deprive the
7 trust of a tax benefit or impose a tax burden not described in subsection (c) of
8 this section. The release may be permanent or for a specified period, including
9 a period measured by the life of an individual.

10 (f) Terms of a trust that limit the power of a trustee to make an adjustment
11 between principal and income do not affect the application of this section
12 unless it is clear from the terms of the trust that the terms are intended to deny
13 the trustee the power of adjustment conferred by subsection (a) of this section.

14 § 3325. JUDICIAL CONTROL OF DISCRETIONARY POWER

15 (a) The court may not order a fiduciary to change a decision to exercise or
16 not to exercise a discretionary power conferred by this chapter unless it
17 determines that the decision was an abuse of the fiduciary's discretion. A
18 fiduciary's decision is not an abuse of discretion merely because the court
19 would have exercised the power in a different manner or would not have
20 exercised the power.

1 (b) The decisions to which subsection (a) of this section applies include:

2 (1) a decision under subsection 3324(a) of this title as to whether and to
3 what extent an amount should be transferred from principal to income or from
4 income to principal.

5 (2) a decision regarding the factors that are relevant to the trust and its
6 beneficiaries, the extent to which the factors are relevant, and the weight, if
7 any, to be given to those factors, in deciding whether and to what extent to
8 exercise the discretionary power conferred by subsection 3324(a) of this title.

9 (c) If the court determines that a fiduciary has abused the fiduciary's
10 discretion, the court may place the income and remainder beneficiaries in the
11 positions they would have occupied if the discretion had not been abused,
12 according to the following rules:

13 (1) To the extent that the abuse of discretion has resulted in no
14 distribution to a beneficiary or in a distribution that is too small, the court shall
15 order the fiduciary to distribute from the trust to the beneficiary an amount that
16 the court determines will restore the beneficiary, in whole or in part, to the
17 beneficiary's appropriate position.

18 (2) To the extent that the abuse of discretion has resulted in a
19 distribution to a beneficiary which is too large, the court shall place the
20 beneficiaries, the trust, or both, in whole or in part, in their appropriate
21 positions by ordering the fiduciary to withhold an amount from one or more

1 future distributions to the beneficiary who received the distribution that was
2 too large or ordering that beneficiary to return some or all of the distribution to
3 the trust.

4 (3) To the extent that the court is unable, after applying subdivisions (1)
5 and (2) of this subsection, to place the beneficiaries or the trust or both in the
6 positions they would have occupied if the discretion had not been abused, the
7 court may order the fiduciary to pay an appropriate amount from its own funds
8 to one or more of the beneficiaries or the trust or both.

9 (d) Upon petition by the fiduciary, the court having jurisdiction over a trust
10 or estate shall determine whether a proposed exercise or nonexercise by the
11 fiduciary of a discretionary power conferred by this chapter will result in an
12 abuse of the fiduciary's discretion. If the petition describes the proposed
13 exercise or nonexercise of the power and contains sufficient information to
14 inform the beneficiaries of the reasons for the proposal, the facts upon which
15 the fiduciary relies, and an explanation of how the income and remainder
16 beneficiaries will be affected by the proposed exercise or nonexercise of the
17 power, a beneficiary who challenges the proposed exercise or nonexercise has
18 the burden of establishing that it will result in an abuse of discretion.

1 § 3326. UNIFORMITY OF APPLICATION AND CONSTRUCTION

2 In applying and construing this chapter, consideration shall be given to the
3 need to promote uniformity of the law with respect to its subject matter among
4 states that enact it.

5 § 3327. SEVERABILITY CLAUSE

6 If any provision of this chapter or its application to any person or
7 circumstance is held invalid, the invalidity does not affect other provisions or
8 applications of this chapter which can be given effect without the invalid
9 provision or application, and to this end the provisions of this chapter are
10 severable.

11 Subchapter 2. Decedent's Estate or Terminating Income Interest

12 § 3331. DETERMINATION AND DISTRIBUTION OF NET INCOME

13 After a decedent dies, in the case of an estate, or after an income interest in
14 a trust ends, the following rules apply:

15 (1) A fiduciary of an estate or of a terminating income interest shall
16 determine the amount of net income and net principal receipts received from
17 property specifically given to a beneficiary under the rules in subchapters 3, 4,
18 and 5 of this chapter which apply to trustees and under the rules in
19 subdivision (5) of this section. The fiduciary shall distribute the net income
20 and net principal receipts to the beneficiary who is to receive the specific
21 property.

1 (2) A fiduciary shall determine the remaining net income of a
2 decedent's estate or a terminating income interest under the rules in
3 subchapters 3, 4, and 5 of this chapter which apply to trustees and by:

4 (A) including in net income all income from property used to
5 discharge liabilities;

6 (B) paying from income or principal, in the fiduciary's discretion,
7 fees of attorneys, accountants, and fiduciaries; court costs and other expenses
8 of administration; and interest on death taxes, but the fiduciary may pay those
9 expenses from income of property passing to a trust for which the fiduciary
10 claims an estate tax marital or charitable deduction only to the extent that the
11 payment of those expenses from income will not cause the reduction or loss of
12 the deduction; and

13 (C) paying from principal all other disbursements made or incurred in
14 connection with the settlement of a decedent's estate or the winding up of a
15 terminating income interest, including debts, funeral expenses, disposition of
16 remains, family allowances, and death taxes and related penalties that are
17 apportioned to the estate or terminating income interest by the will, the terms
18 of the trust, or applicable law.

19 (3) Unless the will or trust instrument otherwise provides, or the court
20 otherwise directs, a fiduciary shall distribute to a beneficiary who receives a
21 pecuniary amount outright interest from the date that is one year following the

1 date of death of the person whose death gives rise to the payment of the
2 pecuniary bequest or the happening of the contingency that causes the income
3 interest to end, from net income determined under subdivision (2) of this
4 section or from principal to the extent that net income is insufficient.

5 However, this subdivision shall not apply to a pecuniary bequest:

6 (A) to or for the benefit of a decedent's surviving spouse that is or
7 can be qualified for the federal estate tax marital deduction; or

8 (B) to or for the benefit of charitable organizations that are qualified
9 for the federal estate tax charitable deduction, including a charitable remainder
10 trust.

11 (4) A fiduciary shall distribute the net income remaining after
12 distributions required by subdivision (3) of this section in the manner described
13 in section 3332 of this title to all other beneficiaries.

14 (5) A fiduciary may not reduce principal or income receipts from
15 property described in subdivision (1) of this section because of a payment
16 described in section 3371 or 3372 of this title to the extent that the will, the
17 terms of the trust, or applicable law requires the fiduciary to make the payment
18 from assets other than the property or to the extent that the fiduciary recovers
19 or expects to recover the payment from a third party. The net income and
20 principal receipts from the property are determined by including all of the
21 amounts the fiduciary receives or pays with respect to the property, whether

1 those amounts accrued or became due before, on, or after the date of a
2 decedent's death or an income interest's terminating event, and by making a
3 reasonable provision for amounts that the fiduciary believes the estate or
4 terminating income interest may become obligated to pay after the property is
5 distributed.

6 § 3332. DISTRIBUTION TO RESIDUARY AND REMAINDER

7 BENEFICIARIES

8 (a) Each beneficiary described in subdivision 3331(4) of this title is entitled
9 to receive a portion of the net income equal to the beneficiary's fractional
10 interest in undistributed principal assets, using values as of the distribution
11 date. If a fiduciary makes more than one distribution of assets to beneficiaries
12 to whom this section applies, each beneficiary, including one who does not
13 receive part of the distribution, is entitled, as of each distribution date, to the
14 beneficiary's fractional interest in the net income the fiduciary has received
15 after the date of death or terminating event or earlier distribution date, but has
16 not distributed as of the current distribution date.

17 (b) In determining a beneficiary's share of net income, the following rules
18 apply:

19 (1) The beneficiary is entitled to receive a portion of the net income
20 equal to the beneficiary's fractional interest in the undistributed principal

1 assets immediately before the distribution date, including assets that later may
2 be sold to meet principal obligations.

3 (2) The beneficiary's fractional interest in the undistributed principal
4 assets must be calculated without regard to property specifically given to a
5 beneficiary and property required to pay pecuniary amounts.

6 (3) The beneficiary's fractional interest in the undistributed principal
7 assets must be calculated on the basis of the aggregate value of those assets as
8 of the distribution date without reducing the value by any unpaid principal
9 obligation.

10 (4) The distribution date for purposes of this section may be the date as
11 of which the fiduciary calculates the value of the assets if that date is
12 reasonably near the date on which assets are actually distributed.

13 (c) If a fiduciary does not distribute all of the collected but undistributed
14 net income to each person as of a distribution date, the fiduciary shall maintain
15 appropriate records showing the interest of each beneficiary in that net income.

16 (d) A fiduciary may apply the rules in this section, to the extent that the
17 fiduciary considers it appropriate, to net gain or loss realized after the date of
18 death or terminating event or earlier distribution date from the disposition of a
19 principal asset if this section applies to the income from the asset.

1 Subchapter 3. Apportionment at Beginning and End of Income Interest

2 § 3341. WHEN RIGHT TO INCOME BEGINS AND ENDS

3 (a) An income beneficiary is entitled to net income from the date on which
4 the income interest begins. An income interest begins on the date specified in
5 the terms of the trust or, if no date is specified, on the date an asset becomes
6 subject to a trust or successive income interest.

7 (b) An asset becomes subject to a trust:

8 (1) on the date it is transferred to the trust in the case of an asset that is
9 transferred to a trust during the transferor's life;

10 (2) on the date of a testator's death in the case of an asset that becomes
11 subject to a trust by reason of a will, even if there is an intervening period of
12 administration of the testator's estate; or

13 (3) on the date of an individual's death in the case of an asset that is
14 transferred to a fiduciary by a third party because of the individual's death.

15 (c) An asset becomes subject to a successive income interest on the day
16 after the preceding income interest ends, as determined under subsection (d) of
17 this section, even if there is an intervening period of administration to wind up
18 the preceding income interest.

19 (d) An income interest ends on the day before an income beneficiary dies
20 or another terminating event occurs, or on the last day of a period during which
21 there is no beneficiary to whom a trustee may distribute income.

1 § 3342. APPORTIONMENT OF RECEIPTS AND DISBURSEMENTS

2 WHEN DECEDENT DIES OR INCOME INTEREST BEGINS

3 (a) A trustee shall allocate an income receipt or disbursement other than
4 one to which subdivision 3331(1) of this title applies to principal if its due date
5 occurs before a decedent dies in the case of an estate or before an income
6 interest begins in the case of a trust or successive income interest.

7 (b) A trustee shall allocate an income receipt or disbursement to income if
8 its due date occurs on or after the date on which a decedent dies or an income
9 interest begins and it is a periodic due date. An income receipt or
10 disbursement must be treated as accruing from day to day if its due date is not
11 periodic or it has no due date. The portion of the receipt or disbursement
12 accruing before the date on which a decedent dies or an income interest begins
13 must be allocated to principal and the balance must be allocated to income.

14 (c) An item of income or an obligation is due on the date the payer is
15 required to make a payment. If a payment date is not stated, there is no due
16 date for the purposes of this chapter. Distributions to shareholders or other
17 owners from an entity to which section 3351 of this title applies are deemed to
18 be due on the date fixed by the entity for determining who is entitled to receive
19 the distribution or, if no date is fixed, on the declaration date for the
20 distribution. A due date is periodic for receipts or disbursements that must be

1 paid at regular intervals under a lease or an obligation to pay interest or if an
2 entity customarily makes distributions at regular intervals.

3 § 3343. APPORTIONMENT WHEN INCOME INTEREST ENDS

4 (a) As used in this section, “undistributed income” means net income
5 received before the date on which an income interest ends. The term does not
6 include an item of income or expense that is due or accrued or net income that
7 has been added or is required to be added to principal under the terms of the
8 trust.

9 (b) When a mandatory income interest ends, the trustee shall pay to a
10 mandatory income beneficiary who survives that date, or the estate of a
11 deceased mandatory income beneficiary whose death causes the interest to end,
12 the beneficiary’s share of the undistributed income that is not disposed of
13 under the terms of the trust unless the beneficiary has an unqualified power to
14 revoke more than five percent of the trust immediately before the income
15 interest ends. In the latter case, the undistributed income from the portion of
16 the trust that may be revoked must be added to principal.

17 (c) When a trustee’s obligation to pay a fixed annuity or a fixed fraction of
18 the value of the trust’s assets ends, the trustee shall prorate the final payment if
19 and to the extent required by applicable law to accomplish a purpose of the
20 trust or its settlor relating to income, gift, estate, or other tax.

1 Subchapter 4. Allocation Of Receipts During Administration Of Trust

2 Part 1. Receipts from Entities

3 § 3351. CHARACTER OF RECEIPTS

4 (a) As used in this section, "entity" means a corporation, partnership,
5 limited liability company, regulated investment company, real estate
6 investment trust, common trust fund, or any other organization in which a
7 trustee has an interest other than a trust or estate to which section 3352 of this
8 title applies, a business or activity to which section 3353 of this title applies, or
9 an asset-backed security to which section 3365 of this title applies.

10 (b) Except as otherwise provided in this section, a trustee shall allocate to
11 income money received from an entity, including reinvested cash dividends.

12 (c) A trustee shall allocate the following receipts from an entity to
13 principal:

14 (1) property other than money, excluding reinvested cash dividends,
15 provided that if the trustee may elect between money and other property as a
16 distribution, property so elected and distributed shall retain its character as
17 income;

18 (2) money received in one distribution or a series of related distributions
19 in exchange for part or all of a trust's interest in the entity;

20 (3) money received in total or partial liquidation of the entity; and

21 (4) money received from an entity that is a regulated investment

1 ~~company or a real estate investment trust if the money distributed is a capital~~
2 ~~gain dividend for federal income tax purposes.~~

(c) A trustee shall allocate the following receipts from an entity to principal:

(1) property other than money, excluding reinvested cash dividends, provided that if the trustee may elect between money and other property as a distribution, property so elected and distributed shall retain its character as income;

(2) money received in one distribution or a series of related distributions in exchange for part or all of a trust's interest in the entity;

(3) money received in total or partial liquidation of the entity;

(4) money received from an entity that is a regulated investment company or a real estate investment trust if the money distributed is a capital gain dividend for federal income tax purposes; and

(5) capital gains and capital gains distributions.

3 (d) Money is received in partial liquidation:

4 (1) to the extent that the entity, at or near the time of a distribution,
5 indicates that it is a distribution in partial liquidation; or

6 (2) if the total amount of money and property received in a distribution
7 or series of related distributions is greater than 20 percent of the entity's gross

1 assets, as shown by the entity's year-end financial statements immediately
2 preceding the initial receipt.

3 (e) Money is not received in partial liquidation, nor may it be taken into
4 account under subdivision (d)(2) of this section, to the extent that it does not
5 exceed the amount of income tax that a trustee or beneficiary must pay on
6 taxable income of the entity that distributes the money.

7 (f) A trustee may rely upon a statement made by an entity about the source
8 or character of a distribution if the statement is made at or near the time of
9 distribution by the entity's board of directors or other person or group of
10 persons authorized to exercise powers to pay money or transfer property
11 comparable to those of a corporation's board of directors

12 § 3352. DISTRIBUTION FROM TRUST OR ESTATE

13 A trustee shall allocate to income an amount received as a distribution of
14 income from a trust or an estate, in which the trust has an interest other than a
15 purchased interest, and shall allocate to principal an amount received as a
16 distribution of principal from such a trust or estate. If a trustee purchases an
17 interest in a trust that is an investment entity, or a decedent or donor transfers
18 an interest in such a trust to a trustee, section 3351 or 3365 of this title applies
19 to a receipt from the trust.

20 § 3353. BUSINESS AND OTHER ACTIVITIES CONDUCTED BY
21 TRUSTEE

1 (a) If a trustee who conducts a business or other activity determines that it
2 is in the best interest of all the beneficiaries to account separately for the
3 business or activity instead of accounting for it as part of the trust's general
4 accounting records, the trustee may maintain separate accounting records for
5 its transactions, whether or not its assets are segregated from other trust assets.

6 (b) A trustee who accounts separately for a business or other activity may
7 determine the extent to which its net cash receipts must be retained for working
8 capital, the acquisition or replacement of fixed assets, and other reasonably
9 foreseeable needs of the business or activity, and the extent to which the
10 remaining net cash receipts are accounted for as principal or income in the
11 trust's general accounting records. If a trustee sells assets of the business or
12 other activity, other than in the ordinary course of the business or activity, the
13 trustee shall account for the net amount received as principal in the trust's
14 general accounting records to the extent the trustee determines that the amount
15 received is no longer required in the conduct of the business.

16 (c) Activities for which a trustee may maintain separate accounting records
17 include:

18 (1) retail, manufacturing, service, and other traditional business
19 activities;

20 (2) farming;

21 (3) raising and selling livestock and other animals;

- 1 (4) management of rental properties;
2 (5) extraction of minerals and other natural resources;
3 (6) timber operations; and
4 (7) activities to which section 3364 of this title applies.

5 Part 2. Receipts Not Normally Apportioned

6 § 3354. PRINCIPAL RECEIPTS

7 A trustee shall allocate to principal:

- 8 (1) to the extent not allocated to income under this chapter, assets
9 received from a transferor during the transferor's lifetime, a decedent's estate,
10 a trust with a terminating income interest, or a payer under a contract naming
11 the trust or its trustee as beneficiary;
12 (2) money or other property received from the sale, exchange,
13 liquidation, or change in form of a principal asset, including realized profit,
14 subject to this chapter;
15 (3) amounts recovered from third parties to reimburse the trust because
16 of disbursements described in subdivision 3372(a)(7) of this title or for other
17 reasons to the extent not based on the loss of income;
18 (4) proceeds of property taken by eminent domain, but a separate award
19 made for the loss of income with respect to an accounting period during which
20 a current income beneficiary had a mandatory income interest is income;
21 (5) net income received in an accounting period during which there is no

1 beneficiary to whom a trustee may or must distribute income; and

2 (6) other receipts as provided in sections 3358–3365 of this title.

3 § 3355. RENTAL PROPERTY

4 To the extent that a trustee accounts for receipts from rental property
5 pursuant to this section, the trustee shall allocate to income ~~and~~ *an* amount
6 received as rent of real or personal property, including an amount received for
7 cancellation or renewal of a lease. An amount received as a refundable
8 deposit, including a security deposit or a deposit applied as rent for future
9 periods, must be added to principal and held subject to the terms of the lease
10 and is not available for distribution to a beneficiary until the trustee's
11 contractual obligations have been satisfied with respect to that amount.

12 § 3356. OBLIGATION TO PAY MONEY

13 (a) An amount received as interest, whether determined at a fixed, variable,
14 or floating rate, on a bond or an obligation to pay money to the fiduciary shall
15 be allocated to income.

16 (b) Except as provided in subsections (c) and (d) of this section, a fiduciary
17 shall allocate to principal any gain or loss realized upon the sale or maturity of
18 any bond or obligation to pay money to the fiduciary, regardless of how such
19 bond or other obligation was acquired.

20 (c) A fiduciary shall allocate to income the difference between inventory
21 value or cost and the amount realized upon sale or maturity, if greater, for

1 bonds or other obligations that do not bear interest, regardless of how or when
2 such bond or other obligation was acquired.

3 (d) For bonds or other obligations that are acquired by a fiduciary
4 subsequent to the time the principal was established and whose cost is greater
5 than their par or maturity value, the fiduciary shall amortize periodically out of
6 income the premium paid and, upon sale or maturity, shall allocate to principal
7 any gain or loss realized thereon.

8 (e) This section does not apply to a bond or other obligation to which
9 section 3359, 3360, 3361, 3362, 3364, or 3365 of this title applies.

10 § 3357. INSURANCE POLICIES AND SIMILAR CONTRACTS

11 (a) Except as otherwise provided in subsection (b) of this section, a trustee
12 shall allocate to principal the proceeds of a life insurance policy or other
13 contract in which the trust or its trustee is named as beneficiary, including a
14 contract that insures the trust or its trustee against loss for damage to,
15 destruction of, or loss of title to a trust asset. The trustee shall allocate
16 dividends on an insurance policy to income if the premiums on the policy are
17 paid from income, and to principal if the premiums are paid from principal.

18 (b) A trustee shall allocate to income proceeds of a contract that insures the
19 trustee against loss of occupancy or other use by an income beneficiary, loss of
20 income, or, subject to section 3353 of this title, loss of profits from a business.

21 (c) This section does not apply to a contract to which section 3359 of this

1 title applies.

2 Part 3. Receipts Normally Apportioned

3 § 3358. INSUBSTANTIAL ALLOCATIONS NOT REQUIRED

4 If a trustee determines that an allocation between principal and income
5 required by section 3359, 3360, 3361, 3362, or 3365 of this title is
6 insubstantial, the trustee may allocate the entire amount to principal unless one
7 of the circumstances described in subsection 3324(c) of this title applies to the
8 allocation. This power may be exercised by a cotrustee in the circumstances
9 described in subsection 3324(d) of this title and may be released for the
10 reasons and in the manner described in subsection 3324(e) of this title. An
11 allocation is presumed to be insubstantial if:

12 (1) the amount of the allocation would increase or decrease net income
13 in an accounting period, as determined before the allocation, by less than 10
14 percent; or

15 (2) the value of the asset producing the receipt for which the allocation
16 would be made is less than 10 percent of the total value of the trust's assets at
17 the beginning of the accounting period.

18 ~~§ 3359. DEFERRED COMPENSATION, ANNUITIES, AND SIMILAR~~

19 ~~PAYMENTS~~

20 ~~(a) In this section, "payment" means a payment that a trustee may receive~~
21 ~~over a fixed number of years or during the life of one or more individuals.~~

1 ~~because of services rendered or property transferred to the payer in exchange~~
2 for future payments. The term includes a payment made in money or property
3 from the payer's general assets or from a separate fund created by the payer,
4 including a private or commercial annuity, an individual retirement account,
5 and a pension, profit-sharing, stock-bonus, or stock-ownership plan.

6 (b) To the extent that a payment is characterized as interest or a dividend or
7 a payment made in lieu of interest or a dividend, a trustee shall allocate it to
8 income. The trustee shall allocate to principal the balance of the payment and
9 any other payment received in the same accounting period that is not
10 characterized as interest, a dividend, or an equivalent payment.

11 (c) If no part of a payment is characterized as interest, a dividend, or an
12 equivalent payment, and all or part of the payment is required to be made, a
13 trustee shall allocate to income 10 percent of the part that is required to be
14 made during the accounting period and the balance to principal. If no part of a
15 payment is required to be made or the payment received is the entire amount to
16 which the trustee is entitled, the trustee shall allocate the entire payment to
17 principal. For purposes of this subsection, a payment is not "required to be
18 made" to the extent that it is made because the trustee exercises a right of
19 withdrawal.

20 (d) If, to obtain an estate tax marital deduction for a trust, a trustee must
21 allocate more of a payment to income than provided for by this section, the

1 ~~trustee shall allocate to income the additional amount necessary to obtain the~~
2 ~~marital deduction.~~

3 ~~(e) This section does not apply to payments to which section 3360 of this~~
4 ~~title applies.~~

§ 3359. DEFERRED COMPENSATION, ANNUITIES, AND SIMILAR

PAYMENTS

(a) In this section:

(1) "Payment" means a payment that a trustee may receive over a fixed number of years or during the life of one or more individuals because of services rendered or property transferred to the payer in exchange for future payments. The term includes a payment made in money or property from the payer's general assets or from a separate fund created by the payer. For purposes of subsections (d), (e), (f), and (g) of this section, the term also includes any payment from any separate fund, regardless of the reason for the payment.

(2) "Separate fund" includes a private or commercial annuity, an individual retirement account, and a pension, profit-sharing, stock-bonus, or stock ownership plan.

(b) To the extent that payment is characterized as interest, a dividend, or a payment made in lieu of interest or a dividend, a trustee shall allocate the payment to income. The trustee shall allocate to principal the balance of the

payment and any other payment received in the same accounting period that is not characterized as interest, a dividend, or an equivalent payment.

(c) If no part of a payment is characterized as interest, a dividend, or an equivalent payment and all or part of the payment is required to be made, a trustee shall allocate to income 10 percent of the part that is required to be made during the accounting period and the balance to principal. If no part of a payment is required to be made or the payment received is the entire amount to which the trustee is entitled, the trustee shall allocate the entire payment to principal. For purposes of this subsection, a payment is not required to be made to the extent that it is made because the trustee exercises a right of withdrawal.

(d) Except as otherwise provided in subsection (e) of this section, subsections (f) and (g) of this section apply and subsections (b) and (c) of this section do not apply in determining the allocation of a payment made from a separate fund to:

(1) a trust to which an election to qualify for a marital deduction under Section 2056(b)(7) of the Internal Revenue Code of 1986, as amended, has been made; or

(2) a trust that qualifies for the marital deduction under Section 2056(b)(5) of the Internal Revenue Code of 1986, as amended.

(e) Subsections (d), (f), and (g) of this section do not apply if and to the extent that the series of payments would, without the application of subsection (d), qualify for the marital deduction under Section 2056(b)(7)(C) of the Internal Revenue Code of 1986, as amended.

(f) A trustee shall determine the internal income of each separate fund for the accounting period as if the separate fund were a trust subject to this chapter. Upon request of the surviving spouse, the trustee shall demand that the person administering the separate fund distribute the internal income to the trust. The trustee shall allocate a payment from the separate fund to income to the extent of the internal income of the separate fund and distribute that amount to the surviving spouse. The trustee shall allocate the balance of the payment to principal. Upon request of the surviving spouse, the trustee shall allocate principal to income to the extent the internal income of the separate fund exceeds payments made from the separate fund to the trust during the accounting period.

(g) If a trustee cannot determine the internal income of a separate fund but can determine the value of the separate fund, the internal income of the separate fund is deemed to equal four percent of the fund's value, according to the most recent statement of value preceding the beginning of the accounting period. If the trustee can determine neither the internal income of the separate fund nor the fund's value, the internal income of the fund is deemed to equal

the product of the interest rate and the present value of the expected future payments and determined under Section 7520 of the Internal Revenue Code of 1986, as amended, for the month preceding the accounting period for which the computation is made.

(h) This section does not apply to a payment to which section 3360 of this title applies.

1 § 3360. LIQUIDATING ASSET

2 (a) As used in this section, “liquidating asset” means an asset whose value
3 will diminish or terminate because the asset is expected to produce receipts for
4 a period of limited duration. The term includes a leasehold, patent, copyright,
5 royalty right, and right to receive payments during a period of more than one
6 year under an arrangement that does not provide for the payment of interest on
7 the unpaid balance. The term does not include a payment subject to section
8 3359 of this title, resources subject to section 3361 of this title, timber subject
9 to section 3362 of this title, an activity subject to section 3364 of this title, an
10 asset subject to section 3365 of this title, or any asset for which the trustee
11 establishes a reserve for depreciation under section 3373 of this title.

12 (b) A trustee shall allocate to income 10 percent of the receipts from a
13 liquidating asset and the balance to principal.

1 § 3361. MINERALS, WATER, AND OTHER NATURAL RESOURCES

2 (a) To the extent that a trustee accounts for receipts from an interest in
3 minerals or other natural resources pursuant to this section, the trustee shall
4 allocate them as follows:

5 (1) If received as nominal delay rental or nominal annual rent on a lease,
6 a receipt must be allocated to income.

7 (2) If received from a production payment, a receipt must be allocated to
8 income if and to the extent that the agreement creating the production payment
9 provides a factor for interest or its equivalent. The balance must be allocated
10 to principal.

11 (3) If an amount received as a royalty, shut-in-well payment,
12 take-or-pay payment, bonus, or delay rental is more than nominal, 90 percent
13 must be allocated to principal and the balance to income.

14 (4) If an amount is received from a working interest or any other interest
15 not provided for in subdivision (a)(1), (2), or (3) of this section, 90 percent of
16 the net amount received must be allocated to principal and the balance to
17 income.

18 (b) An amount received on account of an interest in water that is renewable
19 must be allocated to income. If the water is not renewable, 90 percent of the
20 amount must be allocated to principal and the balance to income.

1 (c) This chapter applies whether or not a decedent or donor was extracting
2 minerals, water, or other natural resources before the interest became subject to
3 the trust.

4 (d) If a trust owns an interest in minerals, water, or other natural resources
5 on July 1, ~~2011~~ 2012 , the trustee may allocate receipts from the interest as
6 provided in this chapter or in the manner used by the trustee prior to July 1,
7 ~~2011~~ 2012 . If the trust acquires an interest in minerals, water, or other natural
8 resources after July 1, ~~2011~~ 2012 , the trustee shall allocate receipts from the
9 interest as provided in this chapter.

10 § 3362. TIMBER

11 (a) To the extent that a trustee accounts for receipts from the sale of timber
12 and related products pursuant to this section, the trustee shall allocate the net
13 receipts:

14 (1) to income to the extent that the amount of timber removed from the
15 land does not exceed the rate of growth of the timber during the accounting
16 periods in which a beneficiary has a mandatory income interest;

17 (2) to principal to the extent that the amount of timber removed from the
18 land exceeds the rate of growth of the timber or the net receipts are from the
19 sale of standing timber;

20 (3) to or between income and principal if the net receipts are from the
21 lease of timberland or from a contract to cut timber from land owned by a trust,

1 by determining the amount of timber removed from the land under the lease or
2 contract and applying the rules in subdivisions (a)(1) and (2) of this section; or
3 (4) to principal to the extent that advance payments, bonuses, and other
4 payments are not allocated pursuant to subdivisions (a)(1), (2), or (3) of this
5 section.

6 (b) In determining net receipts to be allocated pursuant to subsection (a) of
7 this section, a trustee shall deduct and transfer to principal a reasonable amount
8 for depletion.

9 (c) This chapter applies whether or not a decedent or transferor was
10 harvesting timber from the property before it become subject to the trust.

11 (d) If a trust owns an interest in timberland on July 1, ~~2011~~ 2012 , the
12 trustee may allocate net receipts from the sale of timber and related products as
13 provided in this chapter or in the manner used by the trustee before July 1,
14 ~~2011~~ 2012 . If the trust acquires an interest in timberland after July 1, ~~2011~~
15 2012 , the trustee shall allocate net receipts from the sale of timber and related
16 products as provided in this chapter.

17 § 3363. PROPERTY NOT PRODUCTIVE OF INCOME

18 (a) If a marital deduction is allowed for all or part of a trust whose assets
19 consist substantially of property that does not provide the spouse with
20 sufficient income from or use of the trust assets, and if the amounts that the
21 trustee transfers from principal to income under section 3324 of this title and

1 distributes to the spouse from principal pursuant to the terms of the trust are
2 insufficient to provide the spouse with the beneficial enjoyment required to
3 obtain the marital deduction, the spouse may require the trustee to make
4 property productive of income, convert property within a reasonable time, or
5 exercise the power conferred by subsection 3324(a) of this title. The trustee
6 may decide which action or combination of actions to take.

7 (b) In cases not governed by subsection (a) of this section, proceeds from
8 the sale or other disposition of an asset are principal without regard to the
9 amount of income the asset produces during any accounting period.

10 § 3364. DERIVATIVES AND OPTIONS

11 (a) As used in this section, “derivative” means a contract or financial
12 instrument or a combination of contracts and financial instruments which
13 gives a trust the right or obligation to participate in some or all changes in
14 the price of a tangible or intangible asset or group of assets, or changes in a
15 rate, an index of prices or rates, or other market indicator for an asset or a
16 group of assets.

17 (b) To the extent that a trustee does not account under section 3353 of this
18 title for transactions in derivatives, the trustee shall allocate to principal
19 receipts from and disbursements made in connection with those transactions.

20 (c) If a trustee grants an option to buy property from the trust, whether or
21 not the trust owns the property when the option is granted, grants an option that

1 permits another person to sell property to the trust, or acquires an option to buy
2 property for the trust or an option to sell an asset owned by the trust, and the
3 trustee or other owner of the asset is required to deliver the asset if the option
4 is exercised, an amount received for granting the option must be allocated to
5 principal. An amount paid to acquire the option must be paid from principal.
6 A gain or loss realized upon the exercise of an option, including an option
7 granted to a settlor of the trust for services rendered, must be allocated to
8 principal.

9 § 3365. ASSET-BACKED SECURITIES

10 (a) As used in this section, “asset-backed security” means an asset whose
11 value is based upon the right it gives the owner to receive distributions from
12 the proceeds of financial assets that provide collateral for the security. The
13 term includes an asset that gives the owner the right to receive from the
14 collateral financial assets only the interest or other current return or only the
15 proceeds other than interest or current return. The term does not include an
16 asset to which section 3351 or 3359 of this title applies.

17 (b) If a trust receives a payment from interest or other current return and
18 from other proceeds of the collateral financial assets, the trustee shall allocate
19 to income the portion of the payment which the payer identifies as being from
20 interest or other current return and shall allocate the balance of the payment to
21 principal.

1 (c) If a trust receives one or more payments in exchange for the trust's
2 entire interest in an asset-backed security in one accounting period, the trustee
3 shall allocate the payments to principal. If a payment is one of a series of
4 payments that will result in the liquidation of the trust's interest in the security
5 over more than one accounting period, the trustee shall allocate 10 percent of
6 the payment to income and the balance to principal.

7 Subchapter 5. Allocation of Disbursements During Administration of Trust
8 § 3371. DISBURSEMENTS FROM INCOME

9 A trustee shall make the following disbursements from income to the extent
10 that they are not disbursements to which subdivision 3331(2)(B) or (C)
11 applies:

12 (1) one-half of the regular compensation of the trustee and of any person
13 providing investment advisory or custodial services to the trustee;

14 (2) one-half of all expenses for accountings, judicial proceedings, or
15 other matters that involve both the income and remainder interests;

16 (3) all of the other ordinary expenses incurred in connection with the
17 administration, management, or preservation of trust property and the
18 distribution of income, including interest, ordinary repairs, regularly recurring
19 taxes assessed against principal, and expenses of a proceeding or other matter
20 that concerns primarily the income interest; and

21 (4) recurring premiums on insurance covering the loss of a principal

1 asset or the loss of income from or use of the asset.

2 § 3372. DISBURSEMENTS FROM PRINCIPAL

3 (a) A trustee shall make the following disbursements from principal:

4 (1) the remaining one-half of the disbursements described in
5 subdivisions 3371(1) and (2) of this title;

6 (2) all of the trustee's compensation calculated on principal as a fee for
7 acceptance, distribution, or termination, and disbursements made to prepare
8 property for sale;

9 (3) payments on the principal of a trust debt;

10 (4) expenses that extend the life of trust property or that change the form
11 of principal to an improvement or accretion to another item of trust property.

12 (5) expenses of a proceeding that concerns primarily principal, including
13 a proceeding to construe the trust or to protect the trust or its property;

14 (6) premiums paid on a policy of insurance not described in subdivision
15 3371(4) of this title of which the trust is the owner and beneficiary;

16 (7) estate, inheritance, and other transfer taxes, including penalties,
17 apportioned to the trust; and

18 (8) disbursements related to environmental matters, including
19 reclamation, assessing environmental conditions, remedying and removing
20 environmental contamination, monitoring remedial activities and the release of
21 substances, preventing future releases of substances, collecting amounts from

1 persons liable or potentially liable for the costs of those activities, penalties
2 imposed under environmental laws or regulations and other payments made to
3 comply with those laws or regulations, statutory or common law claims by
4 third parties, and defending claims based on environmental matters.

5 (b) If a principal asset is encumbered with an obligation that requires
6 income from that asset to be paid directly to the creditor, the trustee shall
7 transfer from principal to income an amount equal to the income paid to the
8 creditor in reduction of the principal balance of the obligation.

9 § 3373. TRANSFERS FROM INCOME TO PRINCIPAL FOR

10 DEPRECIATION

11 (a) As used in this section, “depreciation” means a reduction in value due
12 to wear, tear, decay, corrosion, or gradual obsolescence of a fixed asset having
13 a useful life of more than one year.

14 (b) A trustee may transfer to principal a reasonable amount of the net cash
15 receipts from a principal asset that is subject to depreciation, but may not
16 transfer any amount for depreciation in the following instances:

17 (1) of that portion of real property used or available for use by a
18 beneficiary as a residence or of tangible personal property held or made
19 available for the personal use or enjoyment of a beneficiary;

20 (2) during the administration of a decedent’s estate; or

1 (3) under this section if the trustee is accounting under section 3353 of
2 this title for the business or activity in which the asset is used.

3 (c) An amount transferred to principal need not be held as a separate fund.

4 § 3374. TRANSFERS FROM INCOME TO REIMBURSE PRINCIPAL

5 (a) If a trustee makes or expects to make a principal disbursement
6 described in this section, the trustee may transfer an appropriate amount from
7 income to principal in one or more accounting periods to reimburse principal
8 or to provide a reserve for future principal disbursements.

9 (b) Principal disbursements to which subsection (a) of this section applies
10 include, but are not limited to, the following, but only to the extent that the
11 trustee has not been and does not expect to be reimbursed by a third party:

12 (1) an amount chargeable to income but paid from principal because it is
13 unusually large, including extraordinary repairs;

14 (2) a capital improvement to a principal asset, whether in the form of
15 changes to an existing asset or the construction of a new asset, including
16 special assessments;

17 (3) disbursements made to prepare property for rental, including tenant
18 allowances, leasehold improvements, and broker's commissions;

19 (4) periodic payments on an obligation secured by a principal asset to
20 the extent that the amount transferred from income to principal for depreciation
21 is less than the periodic payments; and

1 (5) disbursements described in subdivision 3372(a)(7) of this title.

2 (c) If the asset whose ownership gives rise to the disbursements becomes
3 subject to a successive income interest after an income interest ends, a trustee
4 may continue to transfer amounts from income to principal as provided in
5 subsection (a) of this section.

6 § 3375. INCOME TAXES

7 (a) A tax required to be paid by a trustee based on receipts allocated to
8 income shall be paid from income.

9 (b) A tax required to be paid by a trustee based on receipts allocated to
10 principal shall be paid from principal, even if the tax is called an income tax by
11 the taxing authority.

12 (c) A tax required to be paid by a trustee on the trust's share of an entity's
13 taxable income shall be paid:

14 (1) from income to the extent that receipts from the entity are allocated
15 only to income;

16 (2) from principal to the extent that receipts from the entity are allocated
17 only to principal;

18 (3) proportionately from principal and income to the extent that receipts
19 from the entity are allocated to both income and principal; and

20 (4) from principal to the extent that the tax exceeds the total receipts
21 from the entity.

1 (d) After applying subsections (a) through (c) of this section, the trustee
2 shall adjust income or principal receipts to the extent that the trust's taxes are
3 reduced because the trust receives a deduction for payments made to a
4 beneficiary.

5 § 3376. ADJUSTMENTS BETWEEN PRINCIPAL AND INCOME

6 BECAUSE OF TAXES

7 (a) A fiduciary may make adjustments between principal and income to
8 offset the shifting of economic interests or tax benefits between income
9 beneficiaries and remainder beneficiaries which arise from:

10 (1) elections and decisions, other than those described in subsection (b)
11 of this section, that the fiduciary makes from time to time regarding tax
12 matters;

13 (2) an income tax or any other tax that is imposed upon the fiduciary or
14 a beneficiary as a result of a transaction involving or a distribution from the
15 estate or trust; or

16 (3) subject to subsection (b) of this section, the ownership by an estate
17 or trust of an interest in an entity whose taxable income, whether or not
18 distributed, is includable in the taxable income of the estate, trust, or a
19 beneficiary.

20 (b) A trustee shall make an adjustment from principal to income to
21 compensate an income beneficiary for taxes paid or payable by the income

1 beneficiary in respect of the taxable income of an entity that is taxable to the
2 income beneficiary but that is distributed to the trustee and allocated to
3 principal.

4 (c) If the amount of an estate tax marital deduction or charitable
5 contribution deduction is reduced because a fiduciary deducts an amount paid
6 from principal for income tax purposes instead of deducting it for estate tax
7 purposes, and as a result estate taxes paid from principal are increased and
8 income taxes paid by an estate, trust, or beneficiary are decreased, each estate,
9 trust, or beneficiary that benefits from the decrease in income tax shall
10 reimburse the principal from which the increase in estate tax is paid. The total
11 reimbursement shall equal the increase in the estate tax to the extent that the
12 principal used to pay the increase would have qualified for a marital deduction
13 or charitable contribution deduction but for the payment. The proportionate
14 share of the reimbursement for each estate, trust, or beneficiary whose income
15 taxes are reduced shall be the same as its proportionate share of the total
16 decrease in income tax. An estate or trust shall reimburse principal from
17 income.

18 Sec. 2. REPEAL

19 Chapter 117 of Title 14 (Uniform Principal and Income Act) is repealed.

1 Sec. 3. EFFECTIVE DATE; APPLICABILITY TO EXISTING TRUSTS
2 AND ESTATES

3 This act shall take effect on July 1, ~~2011~~ 2012 and shall apply to every trust
4 or decedent's estate existing on July 1, ~~2011~~ 2012 except as otherwise
5 expressly provided in the will or terms of the trust or in this act.