

State of South Dakota

EIGHTY-SECOND SESSION
LEGISLATIVE ASSEMBLY, 2007

718N0304

SENATE BILL NO. 99

Introduced by: Senator Knudson and Representative Cutler

1 FOR AN ACT ENTITLED, An Act to adopt the Uniform Principal and Income Act.

2 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF SOUTH DAKOTA:

3 Section 1. Section 101. This Act may be cited as the Uniform Principal and Income Act.

4 Section 2. Section 102. In this Act:

5 (1) "Accounting period" means a calendar year unless another twelve-month period is
6 selected by a fiduciary. The term includes a portion of a calendar year or other
7 twelve-month period that begins when an income interest begins or ends when an
8 income interest ends;

9 (2) "Beneficiary" includes, in the case of a decedent's estate, an heir, legatee, and devisee
10 and, in the case of a trust, an income beneficiary and a remainder beneficiary;

11 (3) "Fiduciary" means a personal representative or a trustee. The term includes an
12 executor, administrator, successor personal representative, special administrator, and
13 a person performing substantially the same function;

14 (4) "Income" means money or property that a fiduciary receives as current return from
15 a principal asset. The term includes a portion of receipts from a sale, exchange, or
16 liquidation of a principal asset, to the extent provided in sections 401 to 415,



1 inclusive, of this Act;

2 (5) "Income beneficiary" means a person to whom net income of a trust is or may be
3 payable;

4 (6) "Income interest" means the right of an income beneficiary to receive all or part of
5 net income, whether the terms of the trust require it to be distributed or authorize it
6 to be distributed in the trustee's discretion;

7 (7) "Mandatory income interest" means the right of an income beneficiary to receive net
8 income that the terms of the trust require the fiduciary to distribute;

9 (8) "Net income" means the total receipts allocated to income during an accounting
10 period minus the disbursements made from income during the period, plus or minus
11 transfers under this Act to or from income during the period;

12 (9) "Person" means an individual, corporation, business trust, estate, trust, partnership,
13 limited liability company, association, joint venture, government; governmental
14 subdivision, agency, or instrumentality; public corporation, or any other legal or
15 commercial entity;

16 (10) "Principal" means property held in trust for distribution to a remainder beneficiary
17 when the trust terminates;

18 (11) "Remainder beneficiary" means a person entitled to receive principal when an income
19 interest ends;

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

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

1 Section 3. Section 103. (a) In allocating receipts and disbursements to or between principal
2 and income, and with respect to any matter within the scope of Articles 2 and 3, a fiduciary:

3 (1) Shall administer a trust or estate in accordance with the terms of the trust or the will,
4 even if there is a different provision in this Act;

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

9 (3) Shall administer a trust or estate in accordance with this Act if the terms of the trust
10 or the will do not contain a different provision or do not give the fiduciary a
11 discretionary power of administration; and

12 (4) Shall add a receipt or charge a disbursement to principal to the extent that the terms
13 of the trust and this Act do not provide a rule for allocating the receipt or
14 disbursement to or between principal and income.

15 (b) In exercising the power to adjust under section 104(a) of this Act or a discretionary
16 power of administration regarding a matter within the scope of this Act, whether granted by the
17 terms of a trust, a will, or this Act, a fiduciary shall administer a trust or estate impartially, based
18 on what is fair and reasonable to all of the beneficiaries, except to the extent that the terms of
19 the trust or the will clearly manifest an intention that the fiduciary shall or may favor one or
20 more of the beneficiaries. A determination in accordance with this Act is presumed to be fair
21 and reasonable to all of the beneficiaries.

22 Section 4. Section 104. (a) A trustee may adjust between principal and income to the extent
23 the trustee considers necessary if the trustee invests and manages trust assets as a prudent
24 investor, the terms of the trust describe the amount that may or must be distributed to a

beneficiary by referring to the trust's income, and the trustee determines, after applying the rules in section 103(a) of this Act, that the trustee is unable to comply with section 103(b) of this Act.

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

- (1) The nature, purpose, and expected duration of the trust;
- (2) The intent of the settlor;
- (3) The identity and circumstances of the beneficiaries;
- (4) The needs for liquidity, regularity of income, and preservation and appreciation of capital;
- (5) The assets held in the trust; the extent to which they consist of financial assets, interests in closely held enterprises, tangible and intangible personal property, or real property; the extent to which an asset is used by a beneficiary; and whether an asset was purchased by the trustee or received from the settlor;
- (6) The net amount allocated to income under the other sections of this Act and the increase or decrease in the value of the principal assets, which the trustee may estimate as to assets for which market values are not readily available;
- (7) Whether and to what extent the terms of the trust give the trustee the power to invade principal or accumulate income or prohibit the trustee from invading principal or accumulating income, and the extent to which the trustee has exercised a power from time to time to invade principal or accumulate income;
- (8) The actual and anticipated effect of economic conditions on principal and income and effects of inflation and deflation; and
- (9) The anticipated tax consequences of an adjustment.

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

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

6 (2) That reduces the actuarial value of the income interest in a trust to which a person
7 transfers property with the intent to qualify for a gift tax exclusion;

8 (3) That changes the amount payable to a beneficiary as a fixed annuity or a fixed
9 fraction of the value of the trust assets;

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

12 (5) If possessing or exercising the power to make an adjustment causes an individual to
13 be treated as the owner of all or part of the trust for income tax purposes, and the
14 individual would not be treated as the owner if the trustee did not possess the power
15 to make an adjustment;

16 (6) If possessing or exercising the power to make an adjustment causes all or part of the
17 trust assets to be included for estate tax purposes in the estate of an individual who
18 has the power to remove a trustee or appoint a trustee, or both, and the assets would
19 not be included in the estate of the individual if the trustee did not possess the power
20 to make an adjustment;

21 (7) If the trustee is a beneficiary of the trust; or

22 (8) If the trustee is not a beneficiary, but the adjustment would benefit the trustee directly
23 or indirectly.

24 (d) If subsection (c)(5), (6), (7), or (8) applies to a trustee and there is more than one trustee,

1 a cotrustee to whom the provision does not apply may make the adjustment unless the exercise
2 of the power by the remaining trustee or trustees is not permitted by the terms of the trust.

3 (e) A trustee may release the entire power conferred by subsection (a) or may release only
4 the power to adjust from income to principal or the power to adjust from principal to income
5 if the trustee is uncertain about whether possessing or exercising the power will cause a result
6 described in subsection (c)(1) through (6) or (c)(8) or if the trustee determines that possessing
7 or exercising the power will or may deprive the trust of a tax benefit or impose a tax burden not
8 described in subsection (c). 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 between principal
11 and income do not affect the application of this section unless it is clear from the terms of the
12 trust that the terms are intended to deny the trustee the power of adjustment conferred by
13 subsection (a).

14 Section 5. Section 105. (a) The court may not order a fiduciary to change a decision to
15 exercise or not to exercise a discretionary power conferred by this Act unless it determines that
16 the decision was an abuse of the fiduciary's discretion. A fiduciary's decision is not an abuse of
17 discretion merely because the court would have exercised the power in a different manner or
18 would not have exercised the power.

19 (b) The decisions to which subsection (a) applies include:

20 (1) A decision under section 104(a) of this Act as to whether and to what extent an
21 amount should be transferred from principal to income or from income to principal;

22 (2) A decision regarding the factors that are relevant to the trust and its beneficiaries, the
23 extent to which the factors are relevant, and the weight, if any, to be given to those
24 factors, in deciding whether and to what extent to exercise the discretionary power

1 conferred by section 104(a) of this Act.

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

5 (1) To the extent that the abuse of discretion has resulted in no distribution to a
6 beneficiary or in a distribution that is too small, the court shall order the fiduciary to
7 distribute from the trust to the beneficiary an amount that the court determines will
8 restore the beneficiary, in whole or in part, to the beneficiary's appropriate position;

9 (2) To the extent that the abuse of discretion has resulted in a distribution to a
10 beneficiary which is too large, the court shall place the beneficiaries, the trust, or
11 both, in whole or in part, in their appropriate positions by ordering the fiduciary to
12 withhold an amount from one or more future distributions to the beneficiary who
13 received the distribution that was too large or ordering that beneficiary to return some
14 or all of the distribution to the trust;

15 (3) To the extent that the court is unable, after applying paragraphs (1) and (2), to place
16 the beneficiaries, the trust, or both, in the positions they would have occupied if the
17 discretion had not been abused, the court may order the fiduciary to pay an
18 appropriate amount from its own funds to one or more of the beneficiaries or the trust
19 or both.

20 (d) Upon petition by the fiduciary, the court having jurisdiction over a trust or estate shall
21 determine whether a proposed exercise or nonexercise by the fiduciary of a discretionary power
22 conferred by this Act will result in an abuse of the fiduciary's discretion. If the petition describes
23 the proposed exercise or nonexercise of the power and contains sufficient information to inform
24 the beneficiaries of the reasons for the proposal, the facts upon which the fiduciary relies, and

1 an explanation of how the income and remainder beneficiaries will be affected by the proposed
2 exercise or nonexercise of the power, a beneficiary who challenges the proposed exercise or
3 nonexercise has the burden of establishing that it will result in an abuse of discretion.

4 Section 6. Section 201. After a decedent dies, in the case of an estate, or after an income
5 interest in a trust ends, the following rules apply:

6 (1) A fiduciary of an estate or of a terminating income interest shall determine the
7 amount of net income and net principal receipts received from property specifically
8 given to a beneficiary under the rules in Articles 3 through 5 which apply to trustees
9 and the rules in paragraph (5). The fiduciary shall distribute the net income and net
10 principal receipts to the beneficiary who is to receive the specific property;

11 (2) A fiduciary shall determine the remaining net income of a decedent's estate or a
12 terminating income interest under the rules in Articles 3 through 5 which apply to
13 trustees and by:

14 (A) Including in net income all income from property used to discharge liabilities;

15 (B) Paying from income or principal, in the fiduciary's discretion, fees of
16 attorneys, accountants, and fiduciaries; court costs and other expenses of
17 administration; and interest on death taxes, but the fiduciary may pay those
18 expenses from income of property passing to a trust for which the fiduciary
19 claims an estate tax marital or charitable deduction only to the extent that the
20 payment of those expenses from income will not cause the reduction or loss
21 of the deduction; and

22 (C) Paying from principal all other disbursements made or incurred in connection
23 with the settlement of a decedent's estate or the winding up of a terminating
24 income interest, including debts, funeral expenses, disposition of remains,

1 family allowances, and death taxes and related penalties that are apportioned
2 to the estate or terminating income interest by the will, the terms of the trust,
3 or applicable law.

4 (3) A fiduciary shall distribute to a beneficiary who receives a pecuniary amount outright
5 the interest or any other amount provided by the will, the terms of the trust, or
6 applicable law from net income determined under paragraph (2) or from principal to
7 the extent that net income is insufficient. If a beneficiary is to receive a pecuniary
8 amount outright from a trust after an income interest ends and no interest or other
9 amount is provided for by the terms of the trust or applicable law, the fiduciary shall
10 distribute the interest or other amount to which the beneficiary would be entitled
11 under applicable law if the pecuniary amount were required to be paid under a will.

12 (4) A fiduciary shall distribute the net income remaining after distributions required by
13 paragraph (3) in the manner described in section 202 of this Act to all other
14 beneficiaries, including a beneficiary who receives a pecuniary amount in trust, even
15 if the beneficiary holds an unqualified power to withdraw assets from the trust or
16 other presently exercisable general power of appointment over the trust.

17 (5) A fiduciary may not reduce principal or income receipts from property described in
18 paragraph (1) because of a payment described in section 501 or 502 of this Act to the
19 extent that the will, the terms of the trust, or applicable law requires the fiduciary to
20 make the payment from assets other than the property or to the extent that the
21 fiduciary recovers or expects to recover the payment from a third party. The net
22 income and principal receipts from the property are determined by including all of
23 the amounts the fiduciary receives or pays with respect to the property, whether those
24 amounts accrued or became due before, on, or after the date of a decedent's death or

1 an income interest's terminating event, and by making a reasonable provision for
2 amounts that the fiduciary believes the estate or terminating income interest may
3 become obligated to pay after the property is distributed.

4 Section 7. Section 202. (a) Unless otherwise provided in the trust instrument, an increase
5 in the value of the following investments owned by any trust is distributable as income when
6 it becomes available for distribution:

- 7 (1) A zero coupon bond;
- 8 (2) An annuity contract before annuitization;
- 9 (3) A life insurance contract before the death of the insured;
- 10 (4) An interest in a common trust fund (as defined under § 584 of the Internal Revenue
11 Code) (26 U.S.C. § 584);
- 12 (5) An interest in a partnership, as defined in § 7701 of the Internal Revenue Code (26
13 U.S.C. § 7701); or
- 14 (6) Any other obligation for the payment of money that is payable at a future time in
15 accordance with a fixed, variable, or discretionary schedule of appreciation in excess
16 of the price at which it was issued.

17 (b) For purposes of this section, the increase in value of an investment described in
18 subsection (a) is available for distribution only if the trustee receives cash on account of the
19 investment.

20 (c) The increase in value of the obligations described in subsection (a) is distributable to the
21 beneficiary who was the income beneficiary at the time of the increase from the first principal
22 cash available or, if none is available, when realized by sale, redemption, or other disposition.
23 If unrealized increase is distributed as income but out of principal, the principal shall be
24 reimbursed from the increase when realized.

1 Section 8. Section 301. (a) An income beneficiary is entitled to net income from the date on
2 which the income interest begins. An income interest begins on the date specified in the terms
3 of the trust or, if no date is specified, on the date an asset becomes subject to a trust or
4 successive income interest.

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

6 (1) On the date it is transferred to the trust in the case of an asset that is transferred to a
7 trust during the transferor's life;

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

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

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

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

19 Section 9. Section 302. (a) A trustee shall allocate an income receipt or disbursement other
20 than one to which section 201(1) of this Act applies to principal if its due date occurs before a
21 decedent dies in the case of an estate or before an income interest begins in the case of a trust
22 or successive income interest.

23 (b) A trustee shall allocate an income receipt or disbursement to income if its due date
24 occurs on or after the date on which a decedent dies or an income interest begins and it is a

1 periodic due date. An income receipt or disbursement must be treated as accruing from day to
2 day if its due date is not periodic or it has no due date. The portion of the receipt or
3 disbursement accruing before the date on which a decedent dies or an income interest begins
4 must be allocated to principal and the balance must be allocated to income.

5 (c) An item of income or an obligation is due on the date the payer is required to make a
6 payment. If a payment date is not stated, there is no due date for the purposes of this Act.
7 Distributions to shareholders or other owners from an entity to which section 401 of this Act
8 applies are deemed to be due on the date fixed by the entity for determining who is entitled to
9 receive the distribution or, if no date is fixed, on the declaration date for the distribution. A due
10 date is periodic for receipts or disbursements that must be paid at regular intervals under a lease
11 or an obligation to pay interest or if an entity customarily makes distributions at regular
12 intervals.

13 Section 10. Section 303. (a) In this section, the term, undistributed income, means net
14 income received before the date on which an income interest ends. The term does not include
15 an item of income or expense that is due or accrued or net income that has been added or is
16 required to be added to principal under the terms of the trust.

17 (b) When a mandatory income interest ends, the trustee shall pay to a mandatory income
18 beneficiary who survives that date, or the estate of a deceased mandatory income beneficiary
19 whose death causes the interest to end, the beneficiary's share of the undistributed income that
20 is not disposed of under the terms of the trust unless the beneficiary has an unqualified power
21 to revoke more than five percent of the trust immediately before the income interest ends. In the
22 latter case, the undistributed income from the portion of the trust that may be revoked must be
23 added to principal.

24 (c) When a trustee's obligation to pay a fixed annuity or a fixed fraction of the value of the

1 trust's assets ends, the trustee shall prorate the final payment if and to the extent required by
2 applicable law to accomplish a purpose of the trust or its settlor relating to income, gift, estate,
3 or other tax requirements.

4 Section 11. Section 401. (a) In this section, the term, entity, means a corporation,
5 partnership, limited liability company, regulated investment company, real estate investment
6 trust, common trust fund, or any other organization in which a trustee has an interest other than
7 a trust or estate to which section 402 of this Act applies, a business or activity to which section
8 403 of this Act applies, or an asset-backed security to which section 415 of this Act applies.

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

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

12 (1) Property other than money;

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

15 (3) Money received in total or partial liquidation of the entity; and

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

19 (d) Money is received in partial liquidation:

20 (1) To the extent that the entity, at or near the time of a distribution, indicates that it is
21 a distribution in partial liquidation; or

22 (2) If the total amount of money and property received in a distribution or series of
23 related distributions is greater than twenty percent of the entity's gross assets, as
24 shown by the entity's year-end financial statements immediately preceding the initial

1 receipt.

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

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

9 Section 12. Section 402. A trustee shall allocate to income an amount received as a
10 distribution of income from a trust or an estate in which the trust has an interest other than a
11 purchased interest, and shall allocate to principal an amount received as a distribution of
12 principal from such a trust or estate. If a trustee purchases an interest in a trust that is an
13 investment entity, or a decedent or donor transfers an interest in such a trust to a trustee, section
14 401 or 415 of this Act applies to a receipt from the trust.

15 Section 13. Section 403. (a) If a trustee who conducts a business or other activity determines
16 that it is in the best interest of all the beneficiaries to account separately for the business or
17 activity instead of accounting for it as part of the trust's general accounting records, the trustee
18 may maintain separate accounting records for its transactions, whether or not its assets are
19 segregated from other trust assets.

20 (b) A trustee who accounts separately for a business or other activity may determine the
21 extent to which its net cash receipts must be retained for working capital, the acquisition or
22 replacement of fixed assets, and other reasonably foreseeable needs of the business or activity,
23 and the extent to which the remaining net cash receipts are accounted for as principal or income
24 in the trust's general accounting records. If a trustee sells assets of the business or other activity,

1 other than in the ordinary course of the business or activity, the trustee shall account for the net
2 amount received as principal in the trust's general accounting records to the extent the trustee
3 determines that the amount received is no longer required in the conduct of the business.

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

5 (1) Retail, manufacturing, service, and other traditional business activities;

6 (2) Farming;

7 (3) Raising and selling livestock and other animals;

8 (4) Management of rental properties;

9 (5) Extraction of minerals and other natural resources;

10 (6) Timber operations; and

11 (7) Activities to which section 414 of this Act applies.

12 Section 14. Section 404. A trustee shall allocate to principal:

13 (1) To the extent not allocated to income under this Act, assets received from a transferor
14 during the transferor's lifetime, a decedent's estate, a trust with a terminating income
15 interest, or a payer under a contract naming the trust or its trustee as beneficiary;

16 (2) Money or other property received from the sale, exchange, liquidation, or change in
17 form of a principal asset, including realized profit, subject to this article;

18 (3) Amounts recovered from third parties to reimburse the trust because of
19 disbursements described in section 502(a)(7) of this Act or for other reasons to the
20 extent not based on the loss of income;

21 (4) Proceeds of property taken by eminent domain, but a separate award made for the
22 loss of income with respect to an accounting period during which a current income
23 beneficiary had a mandatory income interest is income;

24 (5) Net income received in an accounting period during which there is no beneficiary to

1 whom a trustee may or must distribute income; and

2 (6) Other receipts as provided in sections 408 to 415, inclusive, of this Act.

3 Section 15. Section 405. To the extent that a trustee accounts for receipts from rental
4 property pursuant to this section, the trustee shall allocate to income an amount received as rent
5 of real or personal property, including an amount received for cancellation or renewal of a lease.
6 An amount received as a refundable deposit, including a security deposit or a deposit that is to
7 be applied as rent for future periods, must be added to principal and held subject to the terms
8 of the lease and is not available for distribution to a beneficiary until the trustee's contractual
9 obligations have been satisfied with respect to that amount.

10 Section 16. Section 406. (a) An amount received as interest, whether determined at a fixed,
11 variable, or floating rate, on an obligation to pay money to the trustee, including an amount
12 received as consideration for prepaying principal, must be allocated to income without any
13 provision for amortization of premium.

14 (b) A trustee shall allocate to principal an amount received from the sale, redemption, or
15 other disposition of an obligation to pay money to the trustee more than one year after it is
16 purchased or acquired by the trustee, including an obligation whose purchase price or value
17 when it is acquired is less than its value at maturity. If the obligation matures within one year
18 after it is purchased or acquired by the trustee, an amount received in excess of its purchase
19 price or its value when acquired by the trust must be allocated to income.

20 (c) This section does not apply to an obligation to which section 409, 410, 411, 412, 414,
21 or 415 of this Act applies.

22 Section 17. Section 407. (a) Except as otherwise provided in subsection (b), a trustee shall
23 allocate to principal the proceeds of a life insurance policy or other contract in which the trust
24 or its trustee is named as beneficiary, including a contract that insures the trust or its trustee

1 against loss for damage to, destruction of, or loss of title to a trust asset. The trustee shall
2 allocate dividends on an insurance policy to income if the premiums on the policy are paid from
3 income, and to principal if the premiums are paid from principal.

4 (b) A trustee shall allocate to income proceeds of a contract that insures the trustee against
5 loss of occupancy or other use by an income beneficiary, loss of income, or, subject to section
6 403 of this Act, loss of profits from a business.

7 (c) This section does not apply to a contract to which section 409 of this Act applies.

8 Section 18. Section 408. If a trustee determines that an allocation between principal and
9 income required by section 409, 410, 411, 412, or 415 of this Act is insubstantial, the trustee
10 may allocate the entire amount to principal unless one of the circumstances described in section
11 104(c) of this Act applies to the allocation. This power may be exercised by a cotrustee in the
12 circumstances described in section 104(d) of this Act and may be released for the reasons and
13 in the manner described in section 104(e) of this Act. An allocation is presumed to be
14 insubstantial if:

- 15 (1) The amount of the allocation would increase or decrease net income in an accounting
16 period, as determined before the allocation, by less than ten percent; or
17 (2) The value of the asset producing the receipt for which the allocation would be made
18 is less than ten percent of the total value of the trust's assets at the beginning of the
19 accounting period.

20 Section 19. Section 409. (a) In this section, the term, payment, means a payment that a
21 trustee may receive over a fixed number of years or during the life of one or more individuals
22 because of services rendered or property transferred to the payer in exchange for future
23 payments. The term includes a payment made in money or property from the payer's general
24 assets or from a separate fund created by the payer, including a private or commercial annuity,

1 an individual retirement account, and a pension, profit-sharing, stock-bonus, or stock-ownership
2 plan.

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

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

14 (d) If, to obtain an estate tax marital deduction for a trust, a trustee must allocate more of a
15 payment to income than provided for by this section, the trustee shall allocate to income the
16 additional amount necessary to obtain the marital deduction.

17 (e) This section does not apply to payments to which section 410 of this Act applies.

18 Section 20. Section 410. (a) In this section, the term, liquidating asset, means an asset whose
19 value will diminish or terminate because the asset is expected to produce receipts for a period
20 of limited duration. The term includes a leasehold, patent, copyright, royalty right, and right to
21 receive payments during a period of more than one year under an arrangement that does not
22 provide for the payment of interest on the unpaid balance. The term does not include a payment
23 subject to section 409 of this Act, resources subject to section 411 of this Act, timber subject
24 to section 412 of this Act, an activity subject to section 414 of this Act, an asset subject to

1 section 415 of this Act, or any asset for which the trustee establishes a reserve for depreciation
2 under section 503 of this Act.

3 (b) A trustee shall allocate to income ten percent of the receipts from a liquidating asset and
4 the balance to principal.

5 Section 21. Section 411. (a) To the extent that a trustee accounts for receipts from an interest
6 in minerals or other natural resources pursuant to this section, the trustee shall allocate them as
7 follows:

8 (1) If received as nominal delay rental or nominal annual rent on a lease, a receipt must
9 be allocated to income;

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

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

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

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

22 (c) This Act applies whether or not a decedent or donor was extracting minerals, water, or
23 other natural resources before the interest became subject to the trust.

24 (d) If a trust owns an interest in minerals, water, or other natural resources on July 1, 2005,

1 the trustee may allocate receipts from the interest as provided in this Act or in the manner used
2 by the trustee before July 1, 2005. If the trust acquires an interest in minerals, water, or other
3 natural resources after July 1, 2005, the trustee shall allocate receipts from the interest as
4 provided in this Act.

5 Section 22. Section 412. (a) To the extent that a trustee accounts for receipts from the sale
6 of timber and related products pursuant to this section, the trustee shall allocate the net receipts:

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

10 (2) To principal to the extent that the amount of timber removed from the land exceeds
11 the rate of growth of the timber or the net receipts are from the sale of standing
12 timber;

13 (3) To or between income and principal if the net receipts are from the lease of
14 timberland or from a contract to cut timber from land owned by a trust, by
15 determining the amount of timber removed from the land under the lease or contract
16 and applying the rules in paragraphs (1) and (2); or

17 (4) To principal to the extent that advance payments, bonuses, and other payments are
18 not allocated pursuant to paragraph (1), (2), or (3).

19 (b) In determining net receipts to be allocated pursuant to subsection (a), a trustee shall
20 deduct and transfer to principal a reasonable amount for depletion.

21 (c) This Act applies whether or not a decedent or transferor was harvesting timber from the
22 property before it became subject to the trust.

23 (d) If a trust owns an interest in timberland on July 1, 2005, the trustee may allocate net
24 receipts from the sale of timber and related products as provided in this Act or in the manner

1 used by the trustee before July 1, 2005. If the trust acquires an interest in timberland after July 1,
2 2005, the trustee shall allocate net receipts from the sale of timber and related products as
3 provided in this Act.

4 Section 23. Section 413. (a) If a marital deduction is allowed for all or part of a trust whose
5 assets consist substantially of property that does not provide the spouse with sufficient income
6 from or use of the trust assets, and if the amounts that the trustee transfers from principal to
7 income under section 104 of this Act and distributes to the spouse from principal pursuant to
8 the terms of the trust are insufficient to provide the spouse with the beneficial enjoyment
9 required to obtain the marital deduction, the spouse may require the trustee to make property
10 productive of income, convert property within a reasonable time, or exercise the power
11 conferred by section 104(a) of this Act. The trustee may decide which action or combination of
12 actions to take.

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

16 Section 24. Section 414. (a) In this section, the term, derivative, means a contract or
17 financial instrument or a combination of contracts and financial instruments which gives a trust
18 the right or obligation to participate in some or all changes in the price of a tangible or
19 intangible asset or group of assets, or changes in a rate, an index of prices or rates, or other
20 market indicator for an asset or a group of assets.

21 (b) To the extent that a trustee does not account under section 403 of this Act for
22 transactions in derivatives, the trustee shall allocate to principal receipts from and disbursements
23 made in connection with those transactions.

24 (c) If a trustee grants an option to buy property from the trust, whether or not the trust owns

1 the property when the option is granted, grants an option that permits another person to sell
2 property to the trust, or acquires an option to buy property for the trust or an option to sell an
3 asset owned by the trust, and the trustee or other owner of the asset is required to deliver the
4 asset if the option 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. A gain or loss
6 realized upon the exercise of an option, including an option granted to a settlor of the trust for
7 services rendered, must be allocated to principal.

8 Section 25. Section 415. (a) In this section, the term, asset-backed security, means an asset
9 whose value is based upon the right it gives the owner to receive distributions from the proceeds
10 of financial assets that provide collateral for the security. The term includes an asset that gives
11 the owner the right to receive from the collateral financial assets only the interest or other
12 current return or only the proceeds other than interest or current return. The term does not
13 include an asset to which section 401 or 409 of this Act applies.

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

18 (c) If a trust receives one or more payments in exchange for the trust's entire interest in an
19 asset-backed security in one accounting period, the trustee shall allocate the payments to
20 principal. If a payment is one of a series of payments that will result in the liquidation of the
21 trust's interest in the security over more than one accounting period, the trustee shall allocate ten
22 percent of the payment to income and the balance to principal.

23 Section 26. Section 501. A trustee shall make the following disbursements from income to
24 the extent that they are not disbursements to which section 201(2)(B) or (C) of this Act applies:

- 1 (1) One-half of the regular compensation of the trustee and of any person providing
2 investment advisory or custodial services to the trustee;
- 3 (2) One-half of all expenses for accountings, judicial proceedings, or other matters that
4 involve both the income and remainder interests;
- 5 (3) All of the other ordinary expenses incurred in connection with the administration,
6 management, or preservation of trust property and the distribution of income,
7 including interest, ordinary repairs, regularly recurring taxes assessed against
8 principal, and expenses of a proceeding or other matter that concerns primarily the
9 income interest; and
- 10 (4) Recurring premiums on insurance covering the loss of a principal asset or the loss of
11 income from or use of the asset.

12 Section 27. Section 502. (a) A trustee shall make the following disbursements from
13 principal:

- 14 (1) The remaining one-half of the disbursements described in section 501(1) and (2) of
15 this Act;
- 16 (2) All of the trustee's compensation calculated on principal as a fee for acceptance,
17 distribution, or termination, and disbursements made to prepare property for sale;
- 18 (3) Payments on the principal of a trust debt;
- 19 (4) Expenses of a proceeding that concerns primarily principal, including a proceeding
20 to construe the trust or to protect the trust or its property;
- 21 (5) Premiums paid on a policy of insurance not described in section 501(4) of this Act
22 of which the trust is the owner and beneficiary;
- 23 (6) Estate, inheritance, and other transfer taxes, including penalties, apportioned to the
24 trust; and

(7) Disbursements related to environmental matters, including reclamation, assessing environmental conditions, remedying and removing environmental contamination, monitoring remedial activities and the release of substances, preventing future releases of substances, collecting amounts from persons liable or potentially liable for the costs of those activities, penalties imposed under environmental laws or regulations and other payments made to comply with those laws or regulations, statutory or common law claims by third parties, and defending claims based on environmental matters.

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

Section 28. Section 503. a) In this section, the term, depreciation, means a reduction in value due to wear, tear, decay, corrosion, or gradual obsolescence of a fixed asset having a useful life of more than one year.

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

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

(2) During the administration of a decedent's estate; or

(3) Under this section if the trustee is accounting under section 403 of this Act for the business or activity in which the asset is used.

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

Section 29. Section 504. (a) If a trustee makes or expects to make a principal disbursement

1 described in this section, the trustee may transfer an appropriate amount from income to
2 principal in one or more accounting periods to reimburse principal or to provide a reserve for
3 future principal disbursements.

4 (b) Principal disbursements to which subsection (a) applies include the following, but only
5 to the extent that the trustee has not been and does not expect to be reimbursed by a third party:

6 (1) An amount chargeable to income but paid from principal because it is unusually
7 large, including extraordinary repairs;

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

10 (3) Disbursements made to prepare property for rental, including tenant allowances,
11 leasehold improvements, and broker's commissions;

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

15 (5) Disbursements described in section 502(a)(7) of this Act.

16 (c) If the asset whose ownership gives rise to the disbursements becomes subject to a
17 successive income interest after an income interest ends, a trustee may continue to transfer
18 amounts from income to principal as provided in subsection (a).

19 Section 30. Section 505. (a) A tax required to be paid by a trustee based on receipts allocated
20 to income must be paid from income.

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

23 (c) A tax required to be paid by a trustee on the trust's share of an entity's taxable income
24 must be paid proportionately:

- 1 (1) From income to the extent that receipts from the entity are allocated to income; and
- 2 (2) From principal to the extent that:
 - 3 (A) Receipts from the entity are allocated to principal; and
 - 4 (B) The trust's share of the entity's taxable income exceeds the total receipts
 - 5 described in paragraphs (1) and (2)(A).
- 6 (d) For purposes of this section, receipts allocated to principal or income must be reduced
- 7 by the amount distributed to a beneficiary from principal or income for which the trust receives
- 8 a deduction in calculating the tax.
- 9 Section 31. Section 506. (a) A fiduciary may make adjustments between principal and
- 10 income to offset the shifting of economic interests or tax benefits between income beneficiaries
- 11 and remainder beneficiaries which arise from:
 - 12 (1) Elections and decisions, other than those described in subsection (b), that the
 - 13 fiduciary makes from time to time regarding tax matters;
 - 14 (2) An income tax or any other tax that is imposed upon the fiduciary or a beneficiary as
 - 15 a result of a transaction involving or a distribution from the estate or trust; or
 - 16 (3) The ownership by an estate or trust of an interest in an entity whose taxable income,
 - 17 whether or not distributed, is includable in the taxable income of the estate, trust, or
 - 18 a beneficiary.
- 19 (b) If the amount of an estate tax marital deduction or charitable contribution deduction is
- 20 reduced because a fiduciary deducts an amount paid from principal for income tax purposes
- 21 instead of deducting it for estate tax purposes, and as a result estate taxes paid from principal
- 22 are increased and income taxes paid by an estate, trust, or beneficiary are decreased, each estate,
- 23 trust, or beneficiary that benefits from the decrease in income tax shall reimburse the principal
- 24 from which the increase in estate tax is paid. The total reimbursement must equal the increase

1 in the estate tax to the extent that the principal used to pay the increase would have qualified for
2 a marital deduction or charitable contribution deduction but for the payment. The proportionate
3 share of the reimbursement for each estate, trust, or beneficiary whose income taxes are reduced
4 must be the same as its proportionate share of the total decrease in income tax. An estate or trust
5 shall reimburse principal from income.

6 Section 32. Section 601. In applying and construing this Uniform Act, consideration must
7 be given to the need to promote uniformity of the law with respect to its subject matter among
8 states that enact it.

9 Section 33. This Act applies to every trust or will created after July 1, 2007, except as
10 otherwise expressly provided in the will or the terms of the trust or in this act. No trust or
11 decedent's estate based upon a will executed after July 1, 2007, may utilize the provisions of
12 chapter 55-13. Every trust existing on June 30, 2007, or any decedent's estate existing on
13 June 30, 2007, and based upon a will executed prior to July 1, 2007, may elect to apply the
14 provisions of either chapter 55-13 or this act. Such election shall be made by the trustee or
15 personal representative prior to the date of the first income distribution from such trust or estate
16 following July 1, 2007. Such election shall be in writing and notice of such election shall be
17 given in writing to the beneficiaries of the trust or estate, as the case may be.

18 Section 34. Section 605. That chapter 55-13 be amended by adding thereto a NEW
19 SECTION to read as follows:

20 The provisions of this Act may not be utilized by any trust created after June 30, 2007, or
21 by any decedent's estate based upon a will executed subsequent to June 30, 2007. Any trust or
22 decedent's estate not otherwise prohibited by this section from utilizing this chapter may apply
23 the provisions of this chapter to such trust or decedent's estate upon the making of an election
24 as provided in section 33 of this Act.