

## UNIFORM PRINCIPAL AND INCOME ACT

### Footnotes

Chapter applies to every trust or decedent's estate on and after July 1, 2000, except as otherwise provided; see §637.701

### 637.101 Short title.

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

99 Acts, ch 124, §1

### 637.102 Definitions.

As used in this chapter:

1. "*Accounting period*" means a calendar year, unless another twelve-month period is selected by a fiduciary. The term includes a portion of a calendar year or other twelve-month period that begins when an income interest begins or ends when an income interest ends.
2. "*Beneficiary*" includes, in the case of a decedent's estate, an heir, legatee, and devisee, and, in the case of a trust, an income beneficiary and a remainder beneficiary.
3. "*Fiduciary*" means a personal representative or a trustee. The term includes an executor, administrator, successor personal representative, special administrator, and a person performing substantially the same function.
4. "*Income*" means money or property a fiduciary receives as the current return from a principal asset. The term includes a portion of the receipts from a sale, exchange, or liquidation of a principal asset, to the extent provided in subchapter 4.
5. "*Income beneficiary*" means a person to whom a trust's net income is or may be payable.
6. "*Income interest*" means an income beneficiary's right to receive all or part of the net income, whether the terms of the trust require it to be distributed or authorize it to be distributed in the trustee's discretion.
7. "*Mandatory income interest*" means an income beneficiary's right to receive net income that the terms of the trust require the fiduciary to distribute.
8. "*Net income*" means the total receipts allocated to income during an accounting period minus the disbursements made from income during the period. In this definition, receipts and disbursements include items transferred to or from income during the period under this chapter.
9. "*Person*" means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, or any other legal or commercial entity. The term does not include a government or governmental subdivision, agency, or instrumentality.
10. "*Principal*" means property held in trust for distribution to a remainder beneficiary when the trust terminates.
11. "*Remainder beneficiary*" means a person, including another trust, entitled to receive principal when an income interest ends.

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

13. *"Trustee"* includes an original, additional, or successor trustee, whether or not appointed or confirmed by a court.

99 Acts, ch 124, §2

### **637.103 Fiduciary duties general principles.**

1. In allocating receipts and disbursements to or between principal and income, and in any matter within the scope of subchapters 2 and 3, a fiduciary shall do all of the following:

*a.* Administer a trust or estate in accordance with the terms of the trust or the will, even if there is a different provision in this chapter.

*b.* Administer a trust or estate by the exercise of a discretionary power of administration given the fiduciary by the terms of the trust or the will, although the fiduciary may exercise that power in a manner different from a provision of this chapter.

*c.* Administer a trust or estate in accordance with this chapter if the terms of the trust or the will do not contain a different provision or do not give the fiduciary a discretionary power of administration.

*d.* Add a receipt or charge a disbursement to principal to the extent that the terms of the trust and this chapter do not provide a rule for allocating the receipt or disbursement to or between principal and income.

2. In exercising a discretionary power of administration regarding a matter within the scope of this chapter, whether granted by the terms of a trust, a will, or this chapter, a fiduciary shall administer a trust or estate impartially, based on what is fair and reasonable to all of the beneficiaries, unless the terms of the trust or the will clearly manifest an intention that the fiduciary shall or may favor one or more of the beneficiaries. A determination in accordance with this chapter is presumed to be fair and reasonable to all of the beneficiaries.

99 Acts, ch 124, §3

### **637.201 Determination and distribution of net income.**

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

1. A fiduciary of an estate or a terminating income interest shall determine the amount of net income and net principal receipts received from property specifically given to a beneficiary under the rules in subchapters 3 through 5 that apply to trustees, and under the rules in subsection 5. The fiduciary shall distribute the net income and net principal receipts to the beneficiary who is to receive the specific property.

2. A fiduciary shall determine the remaining net income of a decedent's estate or a terminating income interest under the rules in subchapters 3 through 5 that apply to trustees, and by doing the following:

*a.* Including in net income all income from property used to discharge liabilities.

*b.* Paying from income or principal, in the fiduciary's discretion, fees of attorneys, accountants, and fiduciaries; court costs and other expenses of administration; and interest on death taxes, but the fiduciary may pay those expenses from income of property passing to a trust for which the fiduciary claims an estate

tax marital or charitable deduction only to the extent that the payment of those expenses from income will not cause the loss of the deduction.

*c.* Paying from principal all other disbursements made or incurred in connection with the settlement of a decedent's estate or the winding up of a terminating income interest, including debts, funeral expenses, disposition of remains, family allowances, and death taxes and related penalties that are apportioned to the estate or terminating income interest by the will, the terms of the trust, or applicable law.

3. A fiduciary shall distribute to a beneficiary who receives a pecuniary amount outright the amount, if any, provided by the will, the terms of the trust, or applicable law, from net income determined under subsection 2 or from principal to the extent the net income is insufficient. If a beneficiary is to receive a pecuniary amount outright from a trust after an income interest ends and no amount is provided for by the terms of the trust or applicable law, the fiduciary shall distribute the amount to which the beneficiary would be entitled under applicable law if the pecuniary amount were required to be paid under a will.

4. A fiduciary shall distribute the net income remaining after distributions required by subsection 3 in the manner described in section 637.202 to all other beneficiaries, including a beneficiary who receives a pecuniary amount in trust, even if the beneficiary holds an unqualified power to withdraw assets from the trust or other presently exercisable general power of appointment over the trust.

5. A fiduciary shall not reduce principal or income receipts from property described in subsection 1 because of a payment described in section 637.501 or 637.502 to the extent that the will, the terms of the trust, or applicable law requires the fiduciary to make the payment from assets other than the property or to the extent that the fiduciary recovers or expects to recover the payment from a third party. The property's net income and principal receipts are determined by including all of the amounts the fiduciary receives or pays with respect to the property, whether those amounts accrued or became due before, on, or after the date of a decedent's death or an income interest's terminating event, and by making a reasonable provision for amounts that the fiduciary believes the estate or terminating income interest may become obligated to pay after the property is distributed.

99 Acts, ch 124, §4

#### **637.202 Distribution to residuary and remainder beneficiaries.**

1. Each beneficiary described in section 637.201, subsection 4, is entitled to receive a portion of the net income equal to the beneficiary's fractional interest in undistributed principal assets, using values as of the distribution date. If a fiduciary makes more than one distribution of assets to beneficiaries to whom this section applies, each beneficiary, including one who does not receive part of the distribution, is entitled, as of each distribution date, to the net income the fiduciary has received after the date of death or terminating event or earlier distribution date but has not distributed as of the current distribution date.

2. In determining a beneficiary's share of net income, the following rules apply:

*a.* The beneficiary is entitled to receive a portion of the net income equal to the beneficiary's fractional interest in the undistributed principal assets immediately before the distribution date, including assets that later may be sold to meet principal obligations.

*b.* The beneficiary's fractional interest in the undistributed principal assets must be calculated without regard to property specifically given to a beneficiary and property required to pay pecuniary amounts not in trust.

*c.* The beneficiary's fractional interest in the undistributed principal assets must be calculated on the basis of the aggregate value of those assets as of the distribution date without reducing the value by any unpaid principal obligation.

*d.* The distribution date for purposes of this section may be the date as of which the fiduciary calculates the value of the assets if that date is reasonably near the date on which assets are actually distributed.

3. The rules in this section apply to net gain or loss realized after the date of death or terminating event or earlier distribution date from the disposition of a principal asset if this section applies to the income from the asset.

4. If a fiduciary does not distribute all of the collected but undistributed net income or gain to each person as of a distribution date, the fiduciary shall maintain appropriate records showing the interest of each beneficiary in that net income or gain.

99 Acts, ch 124, §5; 2000 Acts, ch 1058, §52

### **637.301 When right to income begins and ends.**

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

2. An asset becomes subject to a trust at the first occurrence of one of the following events:

*a.* On the date it is transferred to the trust in the case of an asset that is transferred to a trust during the transferor's life.

*b.* On the date of a testator's death in the case of an asset that becomes subject to a trust by reason of a will, even if there is an intervening period of administration of the testator's estate.

*c.* On the date of an individual's death in the case of an asset that is transferred to a fiduciary by a third party because of the individual's death.

3. An asset becomes subject to a successive income interest on the day after the preceding income interest ends, as determined under subsection 4, even if there is an intervening period of administration to wind up the preceding income interest.

4. An income interest ends on the day before an income beneficiary dies or another terminating event occurs. For purposes of this chapter, an income interest also ends on the last day of a period during which there is no beneficiary to whom a trustee may distribute income.

99 Acts, ch 124, §6

### **637.302 Apportionment of receipts and disbursements when decedent dies or income interest begins.**

1. An income receipt or disbursement other than one to which section 637.201, subsection 1, applies must be allocated to principal if its due date occurs before a decedent dies in the case of an estate, or before an income interest begins in the case of a trust or successive income interest.

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

3. An item of income or an obligation is due on the date on which the payor is required to make a payment. If

there is no stated payment date, there is no due date for the purposes of this chapter. Distributions to shareholders or other owners from an entity to which section 637.401 applies are deemed to be due on the date fixed by the entity for determining who is entitled to receive the distribution or, if no date is fixed, on the declaration date for the distribution. A due date is periodic for receipts or disbursements that must be paid at regular intervals under a lease or an obligation to pay interest or if an entity customarily makes distributions at regular intervals.

99 Acts, ch 124, §7

### **637.303 Apportionment when income interest ends.**

1. For purposes of this section, "*undistributed income*" means net income received before the date on which an income interest ends. The term does not include an item of income or expense that is due or accrued or net income that has been added or is required to be added to principal pursuant to the terms of the trust.
2. When a mandatory income interest ends, the trustee shall pay to a mandatory income beneficiary who survives that date, or the estate of a deceased mandatory income beneficiary whose death causes the interest to end, the beneficiary's share of the undistributed income that is not disposed of pursuant to the terms of the trust unless the beneficiary has an unqualified power to revoke more than five percent of the trust immediately before the income interest ends. In the latter case, the undistributed income from the portion of the trust that may be revoked must be added to principal.
3. When a trustee's obligation to pay a fixed annuity or a fixed fraction of the value of the trust's assets ends, the trustee shall prorate the final payment if and to the extent required by applicable law to accomplish a purpose of the trust or its settlor relating to income, gift, estate, or other tax requirements.

99 Acts, ch 124, §8

### **637.401 Character of receipts.**

1. For purposes of this section, "*entity*" means a corporation, partnership, joint venture, limited liability company, regulated investment company, real estate investment trust, common trust fund, and any other organization in which a trustee has an interest other than a trust or estate to which section 637.402 applies or a business or activity to which section 637.403 applies.
2. Except as otherwise provided in this section, cash received by a trustee from an entity must be allocated to income.
3. Receipts from an entity which must be allocated to principal include the following items:
  - a. Property other than cash, except as otherwise provided in paragraph "d".
  - b. Cash or property received in one distribution or a series of related distributions in exchange for part or all of a trust's interest in the entity.
  - c. Cash or property received in total or partial liquidation of the entity.
  - d. Cash or property received from an entity that is a regulated investment company or a real estate investment trust if the distribution is a capital gain dividend for federal income tax purposes.
4. Cash or property is received in partial liquidation according to one of the following principles:
  - a. To the extent that the entity, at or near the time of a distribution, indicates that it is a distribution in partial

liquidation.

*b.* If the total amount received in a distribution or series of related distributions is greater than twenty percent of the entity's gross assets, as shown by the entity's year-end financial statements immediately preceding the initial receipt.

5. Cash shall not be received in partial liquidation, nor shall it be taken into account under subsection 4, paragraph "b", to the extent that it does not exceed the amount of income tax that a trustee or beneficiary must pay on taxable income of the entity that distributes the cash.

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

99 Acts, ch 124, §9

#### **637.402 Distribution from trust or estate.**

1. Subject to the terms of a recipient trust, an amount received as a distribution of income from a trust or an estate in which the trust has an interest other than a purchased interest shall be allocated to income.
2. An amount received as a distribution of principal from such a trust or estate shall be allocated to principal.
3. If a trustee purchases an interest in a trust that is an investment entity, or a decedent or donor transfers an interest in such a trust to a trustee, section 637.401 applies to a receipt from the trust.

99 Acts, ch 124, §10

#### **637.403 Business and other activities conducted by trustee.**

1. If a trustee who conducts a business or other activity determines that it is in the best interest of all the beneficiaries to account separately for the business or activity instead of accounting for it as part of the trust's general accounting records, the trustee may maintain separate accounting records for its transactions, whether or not its assets are segregated from other trust assets.
2. A trustee who accounts separately for a business or other activity shall determine the extent to which its net cash receipts must be retained for working capital, the acquisition or replacement of fixed assets, and other reasonably foreseeable needs of the business or activity, and the extent to which the remaining net cash receipts are accounted for as principal or income in the trust's general accounting records. If a trustee sells assets of the business or other activity, other than in the ordinary course of the business or activity, the trustee shall account for the net amount received as principal in the trust's general accounting records to the extent the trustee determines that the amount received is no longer required in the conduct of the business.
3. The trustee may maintain separate accounting records for any of the following activities:
  - a.* Retail, manufacturing, service, and other traditional business activities.
  - b.* Farming.
  - c.* Raising and selling livestock and other animals.
  - d.* Management of rental properties.

*e.* Extraction of minerals and other natural resources.

*f.* Timber operations.

*g.* Activities to which section 637.426 applies.

99 Acts, ch 124, §11

**637.404 through 637.409** Reserved.

**637.410 Principal receipts.**

The following items must be allocated to principal:

1. To the extent not allocated to income under this chapter, assets received from any of the following sources:

*a.* A transferor during the transferor's lifetime.

*b.* A decedent's estate.

*c.* A trust with a terminating income interest.

*d.* A payor pursuant to a contract naming the trust or its trustee as beneficiary.

2. Cash or other property received from the sale, exchange, liquidation, or change in form of a principal asset, including realized profit, subject to this subchapter.

3. Amounts recovered from third parties to reimburse the trust because of disbursements described in section 637.502, subsection 1, paragraph "g", or for other reasons to the extent not based on the loss of income.

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

5. Net income received in a period during which there is no beneficiary to whom a trustee may or must distribute income.

6. Other receipts, as provided in part 3.

99 Acts, ch 124, §12

**637.411 Rental property.**

1. An amount received as rent of real or personal property, including an amount received for cancellation or renewal of a lease, must be allocated to income.

2. An amount received as a refundable deposit, including a security deposit or a deposit that is to be applied as rent for future periods, must be added to principal and held subject to the terms of the lease and is not available for distribution to a beneficiary until the trustee's contractual obligations have been satisfied with respect to that amount.

99 Acts, ch 124, §13

### **637.412 Obligation to pay money.**

1. An amount received as interest, whether determined at a fixed, variable, or floating rate, on an obligation to pay money to the trustee, including an amount received as consideration for prepaying principal, must be allocated to income without any provision for amortization of premium.
2. An amount received from the sale, redemption, or other disposition of an obligation to pay money to the trustee more than one year after it is purchased or acquired by the trustee, including an obligation whose purchase price or value when it is acquired is less than its value at maturity, must be allocated to principal. If the obligation matures within one year after it is purchased or acquired by the trustee, an amount received in excess of its purchase price or its value when acquired by the trust must be allocated to income.
3. This section does not apply to obligations to which sections 637.421 through 637.424, 637.426, and 637.427 apply.

99 Acts, ch 124, §14

### **637.413 Insurance policies and similar contracts.**

1. Proceeds from a life insurance policy whose beneficiary is the trust or its trustee or a policy that insures the trust or its trustee against loss for the damage or destruction of, or loss of title to, a principal asset must be allocated to principal. Dividends received from an insurance policy and the proceeds of any other contract in which the trust or its trustee is named as beneficiary must also be allocated to principal.
2. Insurance proceeds must be allocated to income if they are from a policy that insures the trustee against the loss of occupancy or other use by an income beneficiary, the loss of income, or, subject to section 637.403, the loss of profits from a business.
3. This section does not apply to a contract to which section 637.421 applies.

99 Acts, ch 124, §15

### **637.414 through 637.419 Reserved.**

### **637.420 Insubstantial allocations not required.**

1. If a trustee determines that an allocation between principal and income required by sections 637.421 through 637.424 or section 637.427 is insubstantial, the trustee may allocate the entire receipt to principal.
2. An allocation is presumed to be insubstantial if either of the following would be true if an allocation was made:
  - a. The amount of the allocation would increase or decrease an accounting period's net income, as determined before the allocation, by less than ten percent.
  - b. The value of the asset producing the receipt for which the allocation would be made is less than ten percent of the total value of the trust's assets at the beginning of the accounting period.

99 Acts, ch 124, §16

### **637.421 Deferred compensation, annuities, and similar payments.**

1. This section applies to payments 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 payor in exchange for future payments. The payments include those made in cash or property from the payor's general assets or from a separate fund created by the payor, including a private or commercial annuity, an individual retirement account, and a pension, profit sharing, stock bonus, or stock ownership plan. This section does not apply to payments to which section 637.422 applies.

2. To the extent that a payment is characterized as interest or a dividend or a payment made in lieu of interest or a dividend, it must be allocated to income. 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 must be allocated to principal.

3. 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 ten 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 entire payment must be allocated to principal.

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

99 Acts, ch 124, §17

#### **637.422 Liquidating asset.**

1. In this section, "*liquidating asset*" means an asset whose value will diminish or terminate because the asset is expected to produce receipts for a period of limited duration. The term includes leaseholds, patents, trademarks, copyrights, royalty rights, and rights to receive payments during a period of more than one year under an arrangement that does not provide for the payment of interest on the unpaid balance. The term does not include deferred compensation that is subject to section 637.421, natural resources that are subject to section 637.423, timber that is subject to section 637.424, an activity that is subject to section 637.426, or any asset for which the trustee establishes a reserve for depreciation under section 637.503.

2. A trustee shall allocate to income ten percent of the receipts from a liquidating asset and the balance to principal.

99 Acts, ch 124, §18

#### **637.423 Minerals, water, and other natural resources.**

1. Receipts from an interest in minerals or other natural resources must be allocated according to the type of payment, as follows:

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

b. If received from a production payment, a receipt must be allocated to income to the extent that the agreement creating the production payment provides a factor for interest or its equivalent. The balance must be allocated to principal.

c. If an amount received as a royalty, bonus, or delay rental is more than nominal, ninety percent must be allocated to principal and the balance to income.

d. If an amount is received from a working interest or any other interest not provided for in paragraph "a",

"b", or "c", ninety percent of the net amount received must be allocated to principal and the balance to income.

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

3. This chapter applies without regard to whether a decedent or donor was extracting minerals, water, or other natural resources before the interest became subject to the trust.

4. If a trust owns an interest in minerals, water, or other natural resources on or before July 1, 2000, the trustee may allocate receipts from the interest as provided in this section or in the manner used by the trustee before July 1, 2000. If the trust acquires an interest in minerals, water, or other natural resources after July 1, 2000, the trustee shall allocate receipts from the interest as provided in this section.

99 Acts, ch 124, §19; 2000 Acts, ch 1154, §39

### **637.424 Timber.**

1. A trustee may account for net receipts from the sale of timber and related products under subsection 2 or section 637.403 or, if the trustee determines that net receipts are insubstantial, may allocate the net receipts to principal. The presumptions in section 637.420 apply in determining whether net receipts are insubstantial. If a trust owns more than one block of timberland, the trustee may use different methods to account for net receipts from different blocks.

2. If a trustee does not account under section 637.403 for net receipts from the sale of timber and related products or allocate the net receipts to principal because they are insubstantial, the trustee shall allocate the net receipts according to one of the following rules:

*a.* Allocate the net receipts to income to the extent that the amount of timber removed from the land does not exceed the rate of growth of the block as a whole during the accounting periods in which a beneficiary has a mandatory income interest.

*b.* Allocate the net receipts to principal to the extent that the amount of timber removed from the land exceeds the block's rate of growth or the net receipts are from the sale of standing timber.

*c.* Allocate the net receipts to or between income and principal if the net receipts are from the lease of timberland or from a contract to cut timber from land owned by a trust, by determining the amount of timber removed from the land under the lease or contract and applying the rules in paragraphs "a" and "b".

*d.* Allocate the net receipts to principal to the extent that advance payments, bonuses, and other payments are not allocated pursuant to paragraph "a", "b", or "c".

3. In determining the net receipts from the sale of timber, a trustee shall deduct and transfer to principal a reasonable amount for depletion.

4. This chapter applies regardless of whether a decedent or transferor was harvesting timber from the property before it became subject to the trust.

5. If a trust owns an interest in timberland on or before July 1, 2000, the trustee may allocate net receipts from the sale of timber and related products as provided in this section or in the manner used by the trustee before July 1, 2000. If the trust acquires an interest in timberland after July 1, 2000, the trustee shall allocate net receipts from the sale of timber and related products as provided in this section.

99 Acts, ch 124, §20; 2000 Acts, ch 1154, §40

### **637.425 Property not productive of income.**

1. If a marital deduction is allowed for all or part of a trust whose assets consist substantially of property that does not provide the surviving spouse with sufficient income from or use of the trust assets, the spouse may require the trustee to make property productive of income or convert property within a reasonable time. The trustee may decide which action or combination of actions to take.
2. In all other cases, proceeds from the sale or other disposition of an asset are principal without regard to the amount of income the asset produces during any accounting period.

99 Acts, ch 124, §21

### **637.426 Derivatives and options.**

1. For purposes of this section, "*derivative*" means a contract or financial instrument or a combination of contracts and financial instruments which gives a trust the right or obligation to participate in some or all changes in the price of a tangible or intangible asset or group of assets, or changes in a rate, an index of prices or rates, or other market indicator for an asset or a group of assets.
2. To the extent that a trustee does not account under section 637.403 for transactions in derivatives, receipts from and disbursements made in connection with those transactions must be allocated to principal.
3. If a trustee grants an option to buy property from the trust, whether or not the trust owns the property when the option is granted, grants an option that permits another person to sell property to the trust, or acquires an option to buy property for the trust or an option to sell an asset owned by the trust, and the trustee or other owner of the asset is required to deliver the asset if the option is exercised, an amount received for granting the option must be allocated to principal, and an amount paid to acquire the option must be paid from principal. A gain or loss realized upon the exercise of an option, including an option granted to a settlor of the trust for services rendered, must be allocated to principal.

99 Acts, ch 124, §22

### **637.427 Asset-backed securities.**

1. For purposes of this section, "*asset-backed security*" means an asset whose value is based upon the right it gives the owner to receive distributions from the proceeds of financial assets that provide collateral for the security. The term includes an asset that gives the owner the right to receive only the interest or other current return from the collateral financial assets or only the proceeds from the capital investment in the collateral financial assets. It does not include an asset to which section 637.401 or 637.421 applies.
2. If a trust receives a payment from the interest or other current return and the capital investment of the collateral financial assets, the trustee shall allocate to income the portion of a payment that the payor identifies as being from the interest or other current return, and shall allocate the balance of the payment to principal.
3. If a trust receives one or more payments in exchange for the trust's entire interest in an asset-backed security in one accounting period, the trustee shall allocate the payments to principal. If a payment is one of a series of payments that will result in the liquidation of the trust's interest in the security over more than one accounting period, the trustee shall allocate ten percent of the payment to income and the balance to principal.

**637.501 Disbursements from income.**

A trustee shall make disbursements from income, to the extent that they are not disbursements to which section 637.201, subsection 2, paragraph "b" or "c", applies, according to the following:

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

**637.502 Disbursements from principal.**

1. A trustee shall make disbursements from principal according to the following:
  - a. The remaining one-half of the disbursements described in section 637.501, subsections 1 and 2.
  - b. All of the trustee's compensation calculated on principal as an acceptance, distribution, or termination fee, and disbursements made to prepare property for sale.
  - c. Payments on the principal of a trust debt.
  - d. Expenses of a proceeding that concerns primarily principal, including a proceeding to construe the trust or to protect the trust or its property.
  - e. Insurance premiums paid on a policy not described in section 637.501, subsection 4, of which the trust is the owner and beneficiary.
  - f. Estate, inheritance, and other transfer taxes, including penalties, apportioned to the trust.
  - g. 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.
2. If a trust owns a policy of insurance on the life of an individual and the trust is not the beneficiary of the policy, premiums paid on the policy are a distribution from principal to the policy beneficiary.
3. 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 obligation's principal balance.

99 Acts, ch 124, §25

### **637.503 Transfers from income to principal for depreciation.**

1. For purposes of this section, "*depreciation*" means a reduction in value of a fixed asset having a useful life of more than one year due to wear, tear, decay, corrosion, or gradual obsolescence.
2. A trustee may transfer to principal a reasonable amount of the net cash receipts from a principal asset that is subject to depreciation, but a transfer shall not be made for depreciation under any of the following circumstances:
  - a. When the depreciation involves the portion of real property used or available for use by a beneficiary as a residence, or tangible personal property held or made available for the personal use or enjoyment of a beneficiary.
  - b. When the depreciation occurs during the administration of a decedent's estate.
  - c. If the trustee is accounting under section 637.403 for the business or activity in which the asset is used.
3. An amount transferred to principal need not be held as a separate fund.

99 Acts, ch 124, §26

### **637.504 Transfers from income to reimburse principal.**

1. If a trustee makes or expects to make a principal disbursement described in this section, the trustee may transfer an appropriate amount from income to principal in one or more accounting periods to reimburse principal or to provide a reserve for future principal disbursements.
2. Principal disbursements to which subsection 1 applies include all of the following, but only to the extent that the trustee has not been and does not expect to be reimbursed by a third party:
  - a. An amount chargeable to income but paid from principal because it is unusually large, including extraordinary repairs.
  - b. A capital improvement to a principal asset, whether in the form of changes to an existing asset or the construction of a new asset, including special assessments.
  - c. Disbursements made to prepare property for rental, including leasehold improvements and broker's commissions.
  - d. Periodic payments on an obligation secured by a principal asset to the extent that the amount transferred from income to principal for depreciation is less than the periodic payments.
  - e. Disbursements described in section 637.502, subsection 1, paragraph "g".
3. If the asset whose ownership gives rise to the disbursements becomes subject to a successive income interest after an income interest ends, a trustee may continue to transfer amounts from income to principal as provided in subsection 1.

**637.505 Income taxes.**

1. A tax required to be paid by a trustee based on receipts allocated to income must be paid from income.
2. A tax required to be paid by a trustee based on receipts allocated to principal must be paid from principal, even if the tax is called an income tax by the taxing authority.
3. A tax required to be paid by a trustee on the trust's share of an entity's taxable income must be paid proportionately, according to all of the following principles:
  - a. From income, to the extent that receipts from the entity are allocated to income.
  - b. From principal, to the extent that the following principles are observed:
    - (1) Receipts from the entity are allocated to principal.
    - (2) The trust's share of the entity's taxable income exceeds the total receipts in paragraph "a" and in subparagraph (1).
4. For purposes of this section, receipts allocated to principal or income shall be reduced by the amount distributed to a beneficiary from principal or income for which the trust receives a deduction in calculating the tax.

**637.506 Adjustments between principal and income because of taxes.**

1. A fiduciary may make adjustments between principal and income to offset the shifting of economic interests or tax benefits between income beneficiaries and remainder beneficiaries which arise from any of the following:
  - a. Elections and decisions, other than those described in subsection 2, that the fiduciary makes from time to time regarding tax matters.
  - b. An income tax or any other tax that is imposed upon the fiduciary or a beneficiary as a result of a transaction involving or a distribution from the estate or trust.
  - c. The ownership by an estate or trust of an interest in an entity whose taxable income, whether or not distributed, is includable in the taxable income of the estate, trust, or a beneficiary.
2. If the amount of an estate tax marital deduction or charitable contributions deduction is reduced because a fiduciary deducts an amount that is paid from principal for income tax purposes instead of deducting it for estate tax purposes, and as a result estate taxes paid from principal are increased and income taxes paid by an estate, trust, or beneficiary are decreased, each estate, trust, or beneficiary that benefits from the decrease in income tax shall reimburse the principal from which the increase in estate tax is paid. The total reimbursement must equal the increase in the estate tax to the extent that the principal used to pay the increase would have qualified for a marital deduction or charitable contributions deduction but for the payment. The proportionate share of the reimbursement for each estate, trust, or beneficiary whose income taxes are reduced must be the same as its proportionate share of the total decrease in income tax. An estate or trust shall reimburse principal from income.

**637.601 Definitions.**

For purposes of this subchapter:

1. "*Disinterested person*" means a person who is not a related or subordinate party as defined in section 672(c) of the Internal Revenue Code with respect to the person acting as trustee of the trust and excludes the trustor of the trust and any interested trustee.
2. "*Income trust*" means a trust, created by either an inter vivos or a testamentary instrument, which directs or permits the trustee to distribute the net income of the trust to one or more persons, either in fixed proportions or in amounts or proportions determined by the trustee. However, a trust that does not meet this definition is nonetheless an income trust if the trust is subject to taxation under section 2001 or 2501 of the Internal Revenue Code, until the expiration of the period for filing the return, including extensions.
3. "*Interested distributee*" means a person, to whom distributions of income or principal can currently be made, who has the power to remove the existing trustee and designate as successor a person who may be a related or subordinate party, as defined in section 672(c) of the Internal Revenue Code, with respect to such distributee.
4. "*Interested trustee*" means any of the following:
  - a. An individual trustee to whom the net income or principal of the trust can currently be distributed or would be distributed if the trust were to terminate and be distributed.
  - b. Any trustee who may be removed and replaced by an interested distributee.
  - c. An individual trustee whose legal obligation to support a beneficiary may be satisfied by distributions of income and principal of the trust.
5. "*Total return unitrust*" means an income trust which has been converted under and meets the provisions of this subchapter.
6. "*Trustee*" means a person acting as trustee of the trust, except where expressly noted otherwise, whether acting in the trustee's discretion or on the direction of one or more persons acting in a fiduciary capacity.
7. "*Trustor*" means an individual who creates an inter vivos or a testamentary trust.
8. "*Unitrust amount*" means an amount computed as a percentage of the fair market value of the trust.

99 Acts, ch 124, §30; 2002 Acts, ch 1086, §5, 21; 2003 Acts, ch 108, §110

**637.602 Trustee's authority to convert.**

A trustee, other than an interested trustee, or, where two or more persons are acting as trustee, a majority of the trustees who are not interested trustees, may, in the trustee's sole discretion and without the approval of the court, do any of the following subject to the requirements of section 637.603:

1. Convert an income trust to a total return unitrust.
2. Reconvert a total return unitrust to an income trust.

3. Change the method used to determine the fair market value of the trust.

2002 Acts, ch 1086, §6, 21

**637.603 Trustee requirements to convert or change computation method.**

A trustee may proceed to take action under section 637.602 if all of the following apply:

1. The trustee adopts a written policy for the trust as follows:

*a.* In the case of a trust being administered as an income trust, requiring that future distributions from the trust will be unitrust amounts rather than net income.

*b.* In the case of a trust being administered as a total return unitrust, requiring that future distributions from the trust will be net income rather than unitrust amounts.

*c.* Requiring that the method used to determine the fair market value of the trust will be changed as stated in the policy.

2. The trustee sends written notice of the trustee's intention to take any action described in section 637.602, along with copies of such written policy and this subchapter, to all of the following persons:

*a.* The trustor of the trust, if living.

*b.* All living persons who are currently receiving or eligible to receive distributions of income of the trust.

*c.* All living persons who would receive principal of the trust if the trust were to terminate at the time of the giving of such notice, without regard to the exercise of any power of appointment or, if the trust does not provide for its termination, all living persons who would receive or be eligible to receive distributions of income or principal of the trust if the persons identified in paragraph "b" were deceased.

*d.* All persons named in the governing instrument as adviser to or protector of the trust.

3. At least one person receiving notice under subsection 2, paragraphs "b" and "c", is legally competent.

4. No person receiving such notice under subsection 2, objects, by written instrument delivered to the trustee, to the proposed action of the trustee within sixty days of receipt of such notice.

2002 Acts, ch 1086, §7, 21; 2003 Acts, ch 44, §104

**637.604 Interested trustee's authority to convert.**

If there is no trustee of the trust other than an interested trustee, the interested trustee or, where two or more persons are acting as trustee and are interested trustees, a majority of such interested trustees may, in the trustee's sole discretion and without the approval of the court, do any of the following subject to the requirements of section 637.605:

1. Convert an income trust to a total return unitrust.

2. Reconvert a total return unitrust to an income trust.

3. Change the method used to determine the fair market value of the trust.



**637.605 Interested trustee requirements to convert or change computation method.**

An interested trustee may proceed to take action under section 637.604 if all of the following apply:

1. The trustee adopts a written policy for the trust as follows:
  - a.* In the case of a trust being administered as an income trust, requiring that future distributions from the trust will be unitrust amounts rather than net income.
  - b.* In the case of a trust being administered as a total return unitrust, requiring that future distributions from the trust will be net income rather than unitrust amounts.
  - c.* Requiring that the method used to determine the fair market value of the trust will be changed as stated in the policy.
2. The trustee appoints a disinterested person who, in the person's sole discretion, but acting in a fiduciary capacity, determines for the trustee the method to be used in determining the fair market value of the trust, and which assets, if any, are to be excluded in determining the unitrust amount.
3. The trustee sends written notice of the trustee's intention to take any action described in section 637.604, along with copies of such written policy, this subchapter, and the determination of the disinterested person to all of the following persons:
  - a.* The trustor of the trust, if living.
  - b.* All living persons who are currently receiving or eligible to receive distributions of income of the trust.
  - c.* All living persons who would receive principal of the trust if the trust were to terminate at the time of the giving of such notice, without regard to the exercise of any power of appointment or, if the trust does not provide for its termination, all living persons who would receive or be eligible to receive distributions of income or principal of the trust if the persons identified in paragraph "*b*" were deceased.
  - d.* All persons named in the governing instrument as adviser to or protector of the trust.
4. At least one person receiving notice under subsection 3, paragraphs "*b*" and "*c*", is legally competent.
5. No person receiving the notice described in subsection 3 objects, by written instrument delivered to the trustee, to the proposed action of the trustee within sixty days of receipt of such notice.

2002 Acts, ch 1086, §9, 21; 2003 Acts, ch 44, §105; 2003 Acts, ch 108, §111

**637.606 Petition to court to convert trust.**

If any trustee desires to do any of the following but does not have the ability to or elects not to do so under the provisions of section 637.602 or 637.604, the trustee may petition the court for such order as the trustee deems appropriate:

1. Convert an income trust to a total return unitrust.
2. Reconvert a total return unitrust to an income trust.

3. Change the percentage used to calculate the unitrust amount or the method used to determine the fair market value of the trust.

If, however, there is only one trustee of such trust and such trustee is an interested trustee or in the event there are two or more trustees of such trust and a majority of them are interested trustees, the court, in its own discretion or upon the petition of such trustee or trustees or any person interested in the trust, may appoint a disinterested person who, acting in a fiduciary capacity, shall present such information to the court as necessary to enable the court to make its determinations.

2002 Acts, ch 1086, §10, 21

#### **637.607 Valuation of trust.**

The fair market value of the trust shall be determined at least annually, using such valuation date or dates or averages of valuation dates as are deemed appropriate. Assets for which a fair market value cannot be readily ascertained shall be valued using such valuation methods as are deemed reasonable and appropriate. Such assets may be excluded from valuation, provided all income received with respect to such assets is distributed to the extent distributable in accordance with the terms of the governing instrument.

2002 Acts, ch 1086, §11, 21

#### **637.608 Payout percentage.**

The annual unitrust payout percentage shall be four percent unless the governing instrument specifically provides a different percentage or the court approves a percentage of not less than three percent or more than five percent after notice of intent to seek a payout percentage other than four percent has been given to all of the following persons:

1. The trustor of the trust, if living.
2. All living persons who are currently receiving or eligible to receive distributions of income of the trust.
3. All living persons who would receive principal of the trust if the trust were to terminate at the time of the giving of such notice without regard to the exercise of any power of appointment or, if the trust does not provide for its termination, all living persons who would receive or be eligible to receive distributions of income or principal of the trust if the persons identified in subsection 2 were deceased.
4. All persons named in the governing instrument as adviser to or protector of the trust.

2002 Acts, ch 1086, §12, 21

#### **637.609 Unitrust amount.**

The unitrust amount shall not be less than the net income of the trust, determined without regard to the provisions of section 637.610 for any of the following:

1. A trust for which a marital deduction has been taken for federal tax purposes under section 2056 or 2523 of the Internal Revenue Code, during the lifetime of the spouse for whom the trust was created.
2. A trust to which the generation-skipping transfer tax due under section 2601 of the Internal Revenue Code does not apply by reason of any effective date or transition rule.

2002 Acts, ch 1086, §13, 21

### **637.610 Procedure upon conversion of income trust to total return unitrust.**

Following the conversion of an income trust to a total return unitrust, the trustee:

1. Shall treat the unitrust amount as if it were net income of the trust for purposes of determining the amount available, from time to time, for distribution from the trust.
2. Shall allocate an amount to trust income, not in excess of the annual unitrust payout amount, in the following order:
  - a. The amount derived from net income, as determined if the trust were other than a total return unitrust.
  - b. The amount derived from other ordinary income as determined for federal income tax purposes.
  - c. The amount derived from net realized short-term capital gains as determined for federal income tax purposes.
  - d. The amount derived from net realized long-term capital gains as determined for federal income tax purposes.
  - e. The amount derived from trust principal.

2002 Acts, ch 1086, §14, 21

### **637.611 Total return unitrust administration.**

In administering a total return unitrust, the trustee may, in the trustee's sole discretion but subject to the provisions of the governing instrument, determine all of the following:

1. The effective date of the conversion.
2. The timing of distributions, including provisions for prorating a distribution for a short year in which a beneficiary's right to payments commences or ceases.
3. Whether distributions are to be made in cash or in kind or partly in cash and partly in kind.
4. If the trust is reconverted to an income trust, the effective date of such reconversion.
5. Such other administrative issues as may be necessary or appropriate to carry out the purposes of this subchapter.

2002 Acts, ch 1086, §15, 21

### **637.612 Principal distributions subject to governing instrument.**

Conversion to a total return unitrust under the provisions of this subchapter shall not affect any other provision of the governing instrument, if any, regarding distributions of principal.

2002 Acts, ch 1086, §16, 21

### **637.613 Construction and applicability.**

This subchapter shall be construed as pertaining to the administration of a trust and shall be available to any

trust that is administered in Iowa under Iowa law unless any of the following apply:

1. The governing instrument reflects an intention that the current beneficiary or beneficiaries are to receive an amount other than a reasonable current return from the trust.
2. The trust is a trust described in section 170(f)(2)(B), 664(d), 1361(d), 2702(a)(3), or 2702(b) of the Internal Revenue Code.
3. One or more persons to whom the trustee could distribute income have a power of withdrawal over the trust that is not subject to an ascertainable standard under section 2041 or 2514 of the Internal Revenue Code or that can be exercised to discharge a duty of support the person possesses.
4. The governing instrument expressly prohibits use of this subchapter by specific reference to the subchapter. A provision in the governing instrument that the provisions of sections 637.601 through 637.615 or any corresponding provision of future law shall not be used in the administration of this trust or similar words reflecting such intent shall be sufficient to preclude the use of this subchapter.

2002 Acts, ch 1086, §17, 21

#### **637.614 Good faith actions.**

Any trustee or disinterested person who in good faith takes or fails to take any action under this subchapter shall not be liable to any person affected by such action or inaction, regardless of whether such person received written notice as provided in this subchapter and regardless of whether such person was under a legal disability at the time of the delivery of such notice. Such person's exclusive remedy shall be to obtain an order of the court directing the trustee to convert an income trust to a total return unitrust, or to reconvert a total return unitrust to an income trust.

2002 Acts, ch 1086, §18, 21

#### **637.615 Effective date.**

This subchapter takes effect April 5, 2002, and applies to trusts in existence on that date or created after that date.

2002 Acts, ch 1086, §19, 21

#### **637.701 Application of chapter to existing trusts and estates chapter prevails.**

This chapter applies to every trust or decedent's estate on and after July 1, 2000, except as otherwise expressly provided in the will, the terms of the trust, or this chapter. Notwithstanding any Code provision to the contrary, the provisions of this chapter shall prevail over any other applicable Code provision.

2002 Acts, ch 1086, §20, 21