

Senate Study Bill 1078

SENATE FILE _____
BY (PROPOSED COMMITTEE ON
JUDICIARY BILL BY
CHAIRPERSON REDFERN)

Passed Senate, Date _____ Passed House, Date _____
Vote: Ayes _____ Nays _____ Vote: Ayes _____ Nays _____
Approved _____

A BILL FOR

1 An Act relating to the uniform principal and income Act and a
2 trustee's power to adjust between income and principal.
3 BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF IOWA:
4 TLSB 1408XC 80
5 rh/sh/8

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1 1 Section 1. NEW SECTION. 637.104 TRUSTEE'S POWER TO
1 2 ADJUST.
1 3 1. A trustee may adjust between principal and income to
1 4 the extent the trustee considers necessary if all of the
1 5 following apply:
1 6 a. The trustee invests and manages trust assets as a
1 7 prudent investor.
1 8 b. The terms of the trust describe the amount that may or
1 9 must be distributed to a beneficiary by referring to the
1 10 trust's income.
1 11 c. The trustee determines, after complying with the
1 12 requirements in section 637.103, subsection 1, that the
1 13 trustee is unable to comply with section 637.103, subsection
1 14 2.
1 15 2. In deciding whether and to what extent to exercise the
1 16 power conferred by subsection 1, a trustee shall consider all
1 17 factors relevant to the trust and its beneficiaries, including
1 18 all of the following:
1 19 a. The nature, purpose, and expected duration of the
1 20 trust.
1 21 b. The intent of the settlor.
1 22 c. The identity and circumstances of the beneficiaries.
1 23 d. The need for liquidity, regularity of income, and
1 24 preservation and appreciation of capital.
1 25 e. Assets held in the trust, including all of the
1 26 following:
1 27 (1) The extent to which the assets consist of financial
1 28 assets, interests in closely held enterprises, tangible and
1 29 intangible personal property, or real property.
1 30 (2) The extent to which the asset is used by the
1 31 beneficiary.
1 32 (3) Whether an asset was purchased by the trustee or
1 33 received from the settlor.
1 34 f. The net amount allocated to income under this chapter
1 35 and the increase or decrease in the value of the principal
2 1 assets, which the trustee may estimate as to assets for which
2 2 the market values are not readily available.
2 3 g. Whether and to what extent the terms of the trust give
2 4 the trustee the power to invade principal or accumulate income
2 5 or prohibit the trustee from invading principal or
2 6 accumulating income, and the extent to which the trustee has
2 7 exercised a power to invade principal or accumulate income.
2 8 h. The actual and anticipated effect of economic
2 9 conditions on principal and income and the effects of
2 10 inflation and deflation.
2 11 i. The anticipated tax consequences of an adjustment.
2 12 3. A trustee shall not make an adjustment if any of the
2 13 following apply:
2 14 a. The adjustment diminishes the income interest in a
2 15 trust that requires all of the income to be paid at least
2 16 annually to a spouse and for which an estate tax or gift tax
2 17 marital deduction would be allowed, in whole or in part, if
2 18 the trustee did not have the power to make the adjustment.
2 19 b. The adjustment reduces the actuarial value of the
2 20 income interest in a trust to which a person transfers
2 21 property with the intent to qualify for a gift tax exclusion.
2 22 c. The adjustment changes the amount payable to a

2 23 beneficiary as a fixed annuity or a fixed fraction of the
2 24 value of the trust assets.

2 25 d. The adjustment is from an amount that is permanently
2 26 set aside for charitable purposes under a will or the terms of
2 27 the trust, unless both income and principal are set aside.

2 28 e. If possessing or exercising the power to make an
2 29 adjustment causes an individual to be treated as the owner of
2 30 all or part of the trust for income tax purposes, and the
2 31 individual would not be treated as the owner if the trustee
2 32 did not possess the power to make an adjustment.

2 33 f. If possessing or exercising the power to make an
2 34 adjustment causes all or part of the trust assets to be
2 35 included for estate tax purposes in the estate of an
3 1 individual who has the power to remove a trustee or appoint a
3 2 trustee, or both, and the assets would not be included in the
3 3 estate of the individual if the trustee did not possess the
3 4 power to make an adjustment.

3 5 g. If the trustee is a beneficiary of the trust.

3 6 h. If the trustee is not a beneficiary, but the adjustment
3 7 would benefit the trustee directly or indirectly.

3 8 4. If subsection 3, paragraph "e", "f", "g", or "h",
3 9 applies to a trustee and there is more than one trustee, a
3 10 cotrustee to whom the provision does not apply may make the
3 11 adjustment unless the exercise of the power by the remaining
3 12 trustee or trustees is not permitted by the terms of the
3 13 trust.

3 14 5. A trustee may release the entire power conferred by
3 15 subsection 1 or may release only the power to adjust from
3 16 income to principal or the power to adjust from principal to
3 17 income if the trustee is uncertain about whether possessing or
3 18 exercising the power will cause a result described in
3 19 subsection 3, paragraph "a", "b", "c", "d", "e", "f", or "h",
3 20 or if the trustee determines that possessing or exercising the
3 21 power will or may deprive the trust of a tax benefit or impose
3 22 a tax burden not described in subsection 3. The release may
3 23 be permanent or for a specified period, including a period
3 24 measured by the life of an individual.

3 25 6. Terms of a trust that limit the power of a trustee to
3 26 make an adjustment between principal and income do not affect
3 27 the application of this section unless it is clear from the
3 28 terms of the trust that the terms are intended to deny the
3 29 trustee the power of adjustment conferred by subsection 1.

3 30 Sec. 2. NEW SECTION. 637.105 JUDICIAL CONTROL OF
3 31 DISCRETIONARY POWER.

3 32 1. The court shall not order a fiduciary to change a
3 33 decision to exercise or not to exercise a discretionary power
3 34 conferred by this chapter unless the court determines the
3 35 decision was an abuse of the fiduciary's discretion. A
4 1 fiduciary's decision is not an abuse of discretion merely
4 2 because the court would have exercised the power in a
4 3 different manner or would not have exercised the power.

4 4 2. Subsection 1 shall apply to all of the following:

4 5 a. A decision under section 637.104, subsection 1, as to
4 6 whether and to what extent an amount should be transferred
4 7 from principal to income or from income to principal.

4 8 b. A decision regarding the factors that are relevant to
4 9 the trust and its beneficiaries, the extent to which the
4 10 factors are relevant, and the weight, if any, to be given to
4 11 those factors, in deciding whether and to what extent to
4 12 exercise the discretionary power conferred by section 637.104,
4 13 subsection 1.

4 14 3. If the court determines that a fiduciary has abused the
4 15 fiduciary's discretion, the court may place the income and
4 16 remainder beneficiaries in the positions the beneficiaries
4 17 would have occupied if the discretion had not been abused,
4 18 under the following conditions:

4 19 a. To the extent that the abuse of discretion has resulted
4 20 in no distribution to a beneficiary or in a distribution that
4 21 is too small, the court shall order the fiduciary to
4 22 distribute from the trust to the beneficiary an amount that
4 23 the court determines will restore the beneficiary, in whole or
4 24 in part, to the beneficiary's appropriate position.

4 25 b. To the extent that the abuse of discretion has resulted
4 26 in a distribution to a beneficiary which is too large, the
4 27 court shall place the beneficiaries, the trust, or both, in
4 28 whole or in part, in their appropriate positions by ordering
4 29 the fiduciary to withhold an amount from one or more future
4 30 distributions to the beneficiary who received the distribution
4 31 that was too large or ordering the beneficiary to return some
4 32 or all of the distribution to the trust.

4 33 c. To the extent that the court is unable, after applying

4 34 paragraphs "a" and "b", to place the beneficiaries, the trust,
4 35 or both, in the positions they would have occupied if the
5 1 discretion had not been abused, the court may order the
5 2 fiduciary to pay an appropriate amount from its own funds to
5 3 one or more of the beneficiaries or the trust or both.
5 4 4. Upon the filing of a petition by the fiduciary, the
5 5 court that has jurisdiction over a trust or estate shall
5 6 determine whether a proposed exercise or nonexercise by the
5 7 fiduciary of a discretionary power conferred by this chapter
5 8 will result in an abuse of the fiduciary's discretion. If the
5 9 petition describes the proposed exercise or nonexercise of the
5 10 power and contains sufficient information to inform the
5 11 beneficiaries of the reasons for the proposal, the facts upon
5 12 which the fiduciary relies, and an explanation of how the
5 13 income and remainder beneficiaries will be affected by the
5 14 proposed exercise or nonexercise of the power, a beneficiary
5 15 who challenges the proposed exercise or nonexercise has the
5 16 burden of establishing that it will result in an abuse of
5 17 discretion.

5 18 EXPLANATION

5 19 This bill relates to the uniform principal and income Act
5 20 and a trustee's power to adjust between income and principal.

5 21 The bill allows a trustee to adjust between principal and
5 22 income in order to properly carry out fiduciary duties if all
5 23 of the following conditions are met: the trustee must be
5 24 managing the trust assets under the prudent investor rule, the
5 25 terms of the trust must express the income beneficiary's
5 26 distribution rights in terms of the right to receive income,
5 27 and the trustee must determine whether the trustee is unable
5 28 to administer the trust or estate in an impartial manner. In
5 29 deciding whether and to what extent to exercise the power to
5 30 adjust, the trustee is required to consider certain factors.

5 31 The bill further allows a court to determine whether a
5 32 trustee has abused the trustee's discretion to adjust between
5 33 income and principal. The primary remedy for a finding of an
5 34 abuse of discretion is the restoration of the beneficiaries
5 35 and the trust to the positions they would have occupied if the
6 1 abuse had not occurred. The bill provides a method for a
6 2 court to review a proposed adjustment on petition of the
6 3 trustee.

6 4 LSB 1408XC 80

6 5 rh/sh/8