Senate Fiscal Agency
P. O. Box 30036
Lansing, Michigan 48909-7536

BILL ANALYSIS

Telephone: (517) 373-5383
Fax: (517) 373-1986
TDD: (517) 373-0543

House Bill 5307 (as passed by the House)
Sponsor: Representative William Van Regenmorter
House Committee: Judiciary
Senate Committee: Judiciary

Date Completed: 3-30-04

CONTENT

The bill would create the "Uniform Principal and Income Act" (UPIA) to prescribe the manner in which receipts and expenditures of trusts and estates would have to be credited and charged between income and principal; prescribe the manner in which income would have to be apportioned among beneficiaries at the beginning and upon the termination of a trust or estate; and repeal Public Act 340 of 1965, the Revised Uniform Principal and Income Act.

The bill would take effect on May 1, 2004, and would apply to each trust or descendant's estate existing on that date, except as otherwise expressly provided in the will or terms of the trust or the UPIA. In the application or construction of the UPIA, consideration would have to be given to the need to promote uniformity of the law with respect to the UPIA's subject matter among states that enacted it.

The UPIA would incorporate many current provisions of the Revised Uniform Principal and Income Act as well as several new provisions. These amendments, as described by the National Conference of Commissioners on Uniform State Laws (NCCUSL), which promulgated the model UPIA, are discussed below.

The UPIA would operate only when the governing instrument (e.g., a trust or will) was silent. In allocating receipts and disbursements to or between principal and income, and with respect to other matters addressed by the bill, a fiduciary would have to administer a trust or estate according to the terms of the trust or the will, even if there were a different provision in the UPIA. A fiduciary could administer a trust or estate by exercising discretionary powers of administration granted by the terms of the trust or the will, even if that produced results different from a result required or permitted under the UPIA.

The UPIA would provide specific rules for assets that are not accounted for in the current Act, such as allocating in the same manner the receipts from all entities, including corporations, partnerships, limited liability companies, regulated investment companies, and real estate investment trusts.

Under the UPIA, money received by a fiduciary would be income, unless it fit certain categories. For instance, money received as part of an entity's liquidation, money from an investment company (such as a mutual fund) that labeled a distribution as a capital gain, and property received that was not money (such as a stock distribution) would be allocated as principal under the UPIA. The UPIA provides generally that an income receipt would be principal if it were due before a decedent died, in the case of an estate, or before an income interest began, in the case of a trust. After death or the beginning of an income interest, it would be classified as income.

The UPIA would require the distribution of net income and principal receipts to the appropriate beneficiaries when a decedent died or when an income interest ended. The fiduciary would have discretion to pay certain expenses out of either principal or income unless there were an adverse effect on estate tax marital deductions or income tax charitable deductions. General expenses of an estate would be paid from principal, while a specific pecuniary amount required to be paid, would be paid from income unless the income were insufficient. If any net income remained, it would be distributed to remainder beneficiaries according to their share in principal.

Under the UPIA, a fiduciary would have to use prudent investment rules, and could adjust principal and income to the extent made necessary by prudent investment when a trust provided for a fixed income for the income beneficiary. The current Act does not deal with adjustment as a result of prudent investment.

Generally, the UPIA would provide for payment of ordinary expenses out of income, and for payment of compensation to the fiduciary and legal proceedings from principal and income, and dividing expenses in two between principal and income. A fiduciary could transfer income to principal to make up for an asset's depreciation or to reimburse principal for disbursements that enhanced income (such as repairs to assets that were necessary to maintain income). A fiduciary could adjust principal and income to offset the shifting of economic interests or tax benefits between income and remainder beneficiaries in certain instances.

Under the UPIA, a fiduciary who conducted a business held in a trust could separate out the accounting for the business from that of the trust's other assets. While the current Act treats net profit from a business as income and losses as principal, the UPIA would allow a fiduciary to allocate net cash receipts for working capital, for the acquisition or replacement of fixed assets, and for other reasonably foreseeable business needs.

The UPIA would allow a fiduciary to make adjustments between principal and income for tax purposes. Tax liabilities could accrue to either income or remainder beneficiaries. A fiduciary could make elections under the tax laws and could remedy imbalances that arose because of taxes. The current Act does not provide this discretion to fiduciaries.

The bill would depart from the NCCUSL's model uniform law in regard to factors to be considered when adjustments between principal and income were made. The model uniform law lists several factors that a trustee must consider in deciding whether and to what extent to exercise the power to adjust between principal and income. The bill does not include those factors, but specifies that in exercising discretion to adjust between principal and income, a professional trustee (e.g., a bank) could adopt a policy that applied to all trusts and estates or to individual trusts and estates or classes of trusts and estates, stating whether and under what conditions it would use the adjustment power and the method of making adjustments.

Legislative Analyst: Patrick Affholter

FISCAL IMPACT

To the extent that it would affect the number of disputes over wills and trusts, the bill would have an indeterminate fiscal impact on the judiciary.

Fiscal Analyst: Bethany Wicksall

This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.