

HOUSE BILL No. 5307

November 13, 2003, Introduced by Rep. Van Regenmorter and referred to the Committee on Judiciary.

A bill to enact the uniform principal and income act; to prescribe the manner in which receipts and expenditures of trusts and estates are credited and charged between income and principal, and the manner in which income is apportioned among beneficiaries at the beginning and upon the termination of a trust or estate; to make uniform the law with respect to principal and income allocation; and to repeal acts and parts of acts.

THE PEOPLE OF THE STATE OF MICHIGAN ENACT:

ARTICLE 1

Sec. 101. This act shall be known and may be cited as the "uniform principal and income act".

Sec. 102. As used in this act:

(a) "Accounting period" means a calendar year unless another 12-month period is selected by a fiduciary. Accounting period

HOUSE BILL No. 5307

1 includes a portion of a calendar year or other 12-month period
2 that begins when an income interest begins or ends when an income
3 interest ends.

4 (b) "Beneficiary" means, in the case of a decedent's estate,
5 an heir, legatee, or devisee and, in the case of a trust, an
6 income beneficiary or remainder beneficiary.

7 (c) "Fiduciary" means a personal representative or trustee.
8 Fiduciary includes an executor, administrator, successor personal
9 representative, special personal representative, and a person
10 performing substantially the same function as 1 or more of them.

11 (d) "Income" means money or property that a fiduciary
12 receives as current return from a principal asset. Income
13 includes a portion of receipts from a sale, exchange, or
14 liquidation of a principal asset, to the extent provided in
15 article 4.

16 (e) "Income beneficiary" means a person to whom net income of
17 a trust is or may be payable.

18 (f) "Income interest" means the right of an income
19 beneficiary to receive all or part of net income, whether the
20 terms of the trust require it to be distributed or authorize it
21 to be distributed in the trustee's discretion.

22 (g) "Mandatory income interest" means the right of an income
23 beneficiary to receive net income that the terms of the trust
24 require the fiduciary to distribute.

25 (h) "Net income" means the total receipts allocated to income
26 during an accounting period minus the disbursements made from
27 income during the period, plus or minus transfers under this act

1 to or from income during the period.

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

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

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

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

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

17 Sec. 103. (1) In allocating receipts and disbursements to
18 or between principal and income, and with respect to any matter
19 found within the scope of articles 2 and 3, a fiduciary shall do
20 all of the following:

21 (a) Administer a trust or estate in accordance with the terms
22 of the trust or the will, even if there is a different provision
23 in this act.

24 (b) Administer a trust or estate in accordance with this act
25 if the terms of the trust or the will do not contain a different
26 provision or do not give the fiduciary a discretionary power of
27 administration.

1 (c) Add a receipt or charge a disbursement to principal to
2 the extent that the terms of the trust and this act do not
3 provide a rule for allocating the receipt or disbursement to or
4 between principal and income.

5 (2) A fiduciary may administer a trust or estate by the
6 exercise of a discretionary power of administration given to the
7 fiduciary by the terms of the trust or the will, even if the
8 exercise of the power produces a result different from a result
9 required or permitted under this act.

10 (3) In exercising the power to adjust under section 104 or a
11 discretionary power of administration regarding a matter within
12 the scope of this act, whether granted by the terms of a trust or
13 a will, or as provided in this act, a fiduciary shall administer
14 a trust or estate impartially, based on what is fair and
15 reasonable to all of the beneficiaries, except to the extent that
16 the terms of the trust or the will clearly manifest an intention
17 that the fiduciary shall or may favor 1 or more of the
18 beneficiaries. A determination in accordance with this act is
19 presumed to be fair and reasonable to all of the beneficiaries.

20 Sec. 104. (1) A fiduciary may adjust between principal and
21 income to the extent the fiduciary considers necessary if the
22 fiduciary invests and manages trust or estate assets as a prudent
23 investor, the terms of the trust or will describe the amount that
24 may or must be distributed to a beneficiary by referring to the
25 trust's or estate's income, and the fiduciary determines, after
26 applying the provisions in section 103(1) and (2), that the
27 fiduciary is unable to comply with section 103(3).

1 (2) In deciding whether and to what extent to exercise the
2 power conferred by subsection (1), a fiduciary shall consider all
3 factors relevant to the trust or estate and its beneficiaries.

4 (3) In exercising discretion under this section, a
5 professional trustee may adopt a policy that applies to all
6 trusts and estates, or a policy that applies to individual trusts
7 or estates or classes of trusts or estates, stating whether and
8 under what conditions it will use the adjustment power and the
9 method of making adjustments.

10 (4) A fiduciary shall not make an adjustment that does 1 or
11 more of the following or under 1 or more of the following
12 circumstances:

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

18 (b) Reduces the actuarial value of the income interest in a
19 trust or estate to which a person transfers property with the
20 intent to qualify for a gift tax exclusion.

21 (c) Changes the amount payable to a beneficiary as a fixed
22 annuity or a fixed fraction of the value of the trust or estate
23 assets.

24 (d) Diminishes any amount that is permanently set aside for
25 charitable purposes under a will or the terms of a trust unless
26 both income and principal are so set aside.

27 (e) If possessing or exercising the power to make an

1 adjustment causes an individual to be treated as the owner of all
2 or part of the trust for income tax purposes, and the individual
3 would not be treated as the owner if the trustee did not possess
4 the power to make an adjustment.

5 (f) If possessing or exercising the power to make an
6 adjustment causes all or part of the trust or estate assets to be
7 included for estate tax purposes in the estate of an individual
8 who has the power to remove a fiduciary or appoint a fiduciary,
9 or both, and the assets would not be included in the estate of
10 the individual if the fiduciary did not possess the power to make
11 an adjustment.

12 (g) If the fiduciary is a beneficiary of the trust or
13 estate.

14 (h) If the fiduciary is not a beneficiary, but the adjustment
15 would benefit the fiduciary directly or indirectly.

16 (5) If subsection (4)(e), (f), (g), or (h) applies to a
17 fiduciary and there is more than 1 fiduciary, a cofiduciary to
18 whom the provision does not apply may make the adjustment unless
19 the exercise of the power by the remaining fiduciary or
20 fiduciaries is not permitted by the terms of the trust or will.

21 (6) A fiduciary may release the entire power conferred by
22 subsection (1) or may release only the power to adjust from
23 income to principal or the power to adjust from principal to
24 income if the fiduciary is uncertain about whether possessing or
25 exercising the power will cause a result described in subsection
26 (4)(a) through (f) or (4)(h) or if the fiduciary determines that
27 possessing or exercising the power will or may deprive the trust

House Bill No. 5307 as amended February 3, 2004

1 or estate of a tax benefit or impose a tax burden not described
2 in subsection (4). The release may be permanent or for a
3 specified period, including a period measured by the life of an
4 individual.

5 (7) Terms of a trust or [will] that limit the power of a
6 fiduciary to make an adjustment between principal and income do
7 not affect the application of this section unless it is clear
8 from the terms of the trust or will that the terms are intended
9 to deny the fiduciary the power of adjustment conferred by
10 subsection (1).

11 Sec. 105. (1) The court may not order a fiduciary to change
12 a decision to exercise or not to exercise a discretionary power
13 conferred by this act unless it determines that the decision was
14 an abuse of the fiduciary's discretion. A fiduciary's decision
15 is not an abuse of discretion merely because the court would have
16 exercised the power in a different manner or would not have
17 exercised the power.

18 (2) The decisions to which subsection (1) applies include:

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

22 (b) A decision regarding the factors that are relevant to the
23 trust or estate and its beneficiaries, the extent to which the
24 factors are relevant, and the weight, if any, to be given to
25 those factors, in deciding whether and to what extent to exercise
26 the discretionary power conferred by section 104(1).

27 (c) A decision under section 104(3) to adopt a policy

1 applicable to individual trusts or estates or to classes of
2 trusts or estates.

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

8 (a) To the extent that the abuse of discretion has resulted
9 in no distribution to a beneficiary or in a distribution that is
10 too small, the court shall order the fiduciary to distribute from
11 the trust or estate to the beneficiary an amount that the court
12 determines will restore the beneficiary, in whole or in part, to
13 the beneficiary's appropriate position.

14 (b) To the extent that the abuse of discretion has resulted
15 in a distribution to a beneficiary which is too large, the court
16 shall place the beneficiaries, the trust or estate, or both, in
17 whole or in part, in their appropriate positions by ordering the
18 fiduciary to withhold an amount from 1 or more future
19 distributions to the beneficiary who received the distribution
20 that was too large or ordering that beneficiary to return some or
21 all of the distribution to the trust or estate.

22 (c) To the extent that the court is unable, after applying
23 subdivisions (a) and (b), to place the beneficiaries, the trust
24 or estate, or both, in the positions they would have occupied if
25 the discretion had not been abused, the court may order the
26 fiduciary to pay an appropriate amount from its own funds to 1 or
27 more of the beneficiaries or the trust or estate or both.

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

14

ARTICLE 2

15 Sec. 201. After the settlor dies, in the case of an estate,
16 or after an income interest in a trust ends, all of the following
17 apply:

18 (a) A fiduciary of an estate or of a terminating income
19 interest shall determine the amount of net income and net
20 principal receipts received from property specifically given to a
21 beneficiary under the provisions of articles 3 through 5 that
22 apply to trustees and as provided in subdivision (e). The
23 fiduciary shall distribute the net income and net principal
24 receipts to the beneficiary who is to receive the specific
25 property.

26 (b) A fiduciary shall determine the remaining net income of a
27 decedent's estate or a terminating income interest under the

1 provisions of articles 3 through 5 that apply to trustees and by
2 doing all the following:

3 (i) Including in net income all income from property used to
4 discharge liabilities.

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

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

20 (c) A fiduciary shall distribute to a beneficiary who
21 receives a pecuniary amount outright the interest or any other
22 amount provided by the will, the terms of the trust, or
23 applicable law from net income determined under subdivision (b)
24 or from principal to the extent that net income is insufficient.
25 If a beneficiary is to receive a pecuniary amount outright from a
26 trust after an income interest ends and no interest or other
27 amount is provided for by the terms of the trust or applicable

1 law, the fiduciary shall distribute the interest or other amount
2 to which the beneficiary would be entitled under applicable law
3 if the pecuniary amount were required to be paid under a will.

4 (d) A fiduciary shall distribute the net income remaining
5 after distributions required by subdivision (c) in the manner
6 described in section 202 to all other beneficiaries, including a
7 beneficiary who receives a pecuniary amount in trust, even if the
8 beneficiary holds an unqualified power to withdraw assets from
9 the trust or other presently exercisable general power of
10 appointment over the trust.

11 (e) A fiduciary may not reduce principal or income receipts
12 from property described in subdivision (a) because of a payment
13 or disbursement, or both, described in section 501 or 502 to the
14 extent that the will, the terms of the trust, or applicable law
15 requires the fiduciary to make the payment from assets other than
16 the property or to the extent that the fiduciary recovers or
17 expects to recover the payment from a third party. The net
18 income and principal receipts from the property are determined by
19 including all of the amounts the fiduciary receives or pays with
20 respect to the property, whether those amounts accrued or became
21 due before, on, or after the date of a decedent's death or an
22 income interest's terminating event, and by making a reasonable
23 provision for amounts that the fiduciary believes the estate or
24 terminating income interest may become obligated to pay after the
25 property is distributed.

26 Sec. 202. (1) Each beneficiary described in section 201(d)
27 is entitled to receive a portion of the net income equal to the

1 beneficiary's fractional interest in undistributed principal
2 assets, using values as of the distribution date. For purposes
3 of this section, the fiduciary may estimate the value of assets
4 for which market values are not readily available. If a
5 fiduciary makes more than 1 distribution of assets to
6 beneficiaries to whom this section applies, each beneficiary,
7 including a beneficiary who does not receive part of the
8 distribution, is entitled, as of each distribution date, to the
9 net income the fiduciary has received after the date of death or
10 terminating event or earlier distribution date but has not
11 distributed as of the current distribution date.

12 (2) In determining a beneficiary's share of net income, the
13 following apply:

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

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

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

27 (d) The distribution date for purposes of this section may be

1 the date as of which the fiduciary calculates the value of the
2 assets if that date is reasonably near the date on which assets
3 are actually distributed.

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

8 (4) A fiduciary may apply the provisions in this section, to
9 the extent that the fiduciary considers it appropriate, to net
10 gain or loss realized after the date of death or terminating
11 event or earlier distribution date from the disposition of a
12 principal asset if this section applies to the income from the
13 asset.

14 ARTICLE 3

15 Sec. 301. (1) An income beneficiary is entitled to net
16 income from the date on which the income interest begins. An
17 income interest begins on the date specified in the terms of the
18 trust or, if no date is specified, on the date an asset becomes
19 subject to a trust or successive income interest.

20 (2) An asset becomes subject to a trust on 1 of the
21 following:

22 (a) The date it is transferred to the trust in the case of an
23 asset that is transferred to a trust during the transferor's
24 life.

25 (b) The date of a testator's death in the case of an asset
26 that becomes subject to a trust by reason of a will, even if
27 there is an intervening period of administration of the

1 testator's estate.

2 (c) The date of an individual's death in the case of an asset
3 that is transferred to a fiduciary by a third party because of
4 the individual's death.

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

10 (4) An income interest ends on the day before an income
11 beneficiary dies or another terminating event occurs, or on the
12 last day of a period during which there is no beneficiary to whom
13 a trustee may distribute income.

14 Sec. 302. (1) Except as provided in section 201(a), a
15 trustee shall allocate an income receipt or disbursement to
16 principal if its due date occurs before a settlor dies in the
17 case of an estate or before an income interest begins in the case
18 of a trust or successive income interest.

19 (2) A trustee shall allocate an income receipt or
20 disbursement to income if its due date occurs on or after the
21 date on which the settlor dies or an income interest begins and
22 it is a periodic due date. An income receipt or disbursement
23 shall be treated as accruing from day to day if its due date is
24 not periodic or it has no due date. The portion of the receipt
25 or disbursement accruing before the date on which a settlor dies
26 or an income interest begins shall be allocated to principal and
27 the balance shall be allocated to income.

1 (3) An item of income or an obligation is due on the date the
2 payer is required to make a payment. If a payment date is not
3 stated, there is no due date for the purposes of this act.

4 Distributions to shareholders or other owners from an entity to
5 which section 401 applies are considered to be due on the date
6 fixed by the entity for determining who is entitled to receive
7 the distribution or, if no date is fixed, on the declaration date
8 for the distribution. A due date is periodic for receipts or
9 disbursements that must be paid at regular intervals under a
10 lease or an obligation to pay interest or if an entity
11 customarily makes distributions at regular intervals.

12 Sec. 303. (1) As used in this section, "undistributed
13 income" means net income received before the date on which an
14 income interest ends. Undistributed income does not include an
15 item of income or expense that is due or accrued or net income
16 that has been added or is required to be added to principal under
17 the terms of the trust.

18 (2) Except as otherwise provided in this subsection, when a
19 mandatory income interest ends, the trustee shall pay to a
20 mandatory income beneficiary who survives that date, or the
21 estate of a deceased mandatory income beneficiary whose death
22 causes the interest to end, the beneficiary's share of the
23 undistributed income that is not disposed of under the terms of
24 the trust. If the beneficiary has an unqualified power to revoke
25 more than 5% of the trust immediately before the income interest
26 ends, the undistributed income from the portion of the trust that
27 may be revoked shall be added to principal.

1 (3) When a trustee's obligation to pay a fixed annuity or a
2 fixed fraction of the value of the trust's assets ends, the
3 trustee shall prorate the final payment if and to the extent
4 required by applicable law to accomplish a purpose of the trust
5 or its settlor relating to income, gift, estate, or other tax
6 requirements.

7 ARTICLE 4

8 Sec. 401. (1) As used in this section, "entity" means a
9 corporation, partnership, limited liability company, regulated
10 investment company, real estate investment trust, common trust
11 fund, or other organization in which a trustee has an interest,
12 other than a trust or estate to which section 402 applies, a
13 business or other activity to which section 403 applies, or an
14 asset-backed security to which section 415 applies.

15 (2) Except as otherwise provided in this section, a trustee
16 shall allocate to income money received from an entity.

17 (3) A trustee shall allocate the following receipts from an
18 entity to principal:

19 (a) Property other than money.

20 (b) Money received in 1 distribution or a series of related
21 distributions in exchange for part or all of a trust's interest
22 in the entity.

23 (c) Money received in total liquidation of the entity, or in
24 partial liquidation of the entity as prescribed by subsections
25 (4) and (5).

26 (d) Money received from an entity that is a regulated
27 investment company or a real estate investment trust if the money

1 distributed is a capital gain dividend for federal income tax
2 purposes.

3 (4) Money is received in partial liquidation under either of
4 the following circumstances:

5 (a) To the extent that the entity, at or near the time of a
6 distribution, indicates that it is a distribution in partial
7 liquidation.

8 (b) If the total amount of money and property received in a
9 distribution or series of related distributions is greater than
10 20% of the entity's gross assets, as shown by the entity's
11 year-end financial statements immediately preceding the initial
12 receipt.

13 (5) Money is not received in partial liquidation, nor may it
14 be taken into account under subsection (4)(b), to the extent that
15 it does not exceed the amount of income tax that a trustee or
16 beneficiary must pay on taxable income of the entity that
17 distributes the money.

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

24 Sec. 402. A trustee shall allocate to income an amount
25 received as a distribution of income from a trust or an estate in
26 which the trust has an interest other than a purchased interest,
27 and shall allocate to principal an amount received as a

1 distribution of principal from such a trust or estate. If a
2 trustee purchases an interest in a trust that is an investment
3 entity, or a decedent or donor transfers an interest in such a
4 trust to a trustee, section 401 or 415 applies to a receipt from
5 the trust.

6 Sec. 403. (1) If a trustee who conducts a business or other
7 activity determines that it is in the best interest of all the
8 beneficiaries to account separately for the business or activity
9 instead of accounting for it as part of the trust's general
10 accounting records, the trustee may maintain separate accounting
11 records for its transactions, whether or not its assets are
12 segregated from other trust assets.

13 (2) A trustee who accounts separately for a business or other
14 activity may determine the extent to which its net cash receipts
15 shall be retained for working capital, the acquisition or
16 replacement of fixed assets, and other reasonably foreseeable
17 needs of the business or activity, and the extent to which the
18 remaining net cash receipts are accounted for as principal or
19 income in the trust's general accounting records. If a trustee
20 sells assets of the business or other activity, other than in the
21 ordinary course of the business or activity, the trustee shall
22 account for the net amount received as principal in the trust's
23 general accounting records to the extent the trustee determines
24 that the amount received is no longer required in the conduct of
25 business.

26 (3) A business or other activity for which a trustee may
27 maintain separate accounting records include all of the

1 following:

2 (a) A retail, manufacturing, service, and other traditional
3 business activity.

4 (b) Farming.

5 (c) Raising and selling livestock and other animals.

6 (d) Management of rental property.

7 (e) Extraction of minerals and other natural resources.

8 (f) A timber operation.

9 (g) An activity to which section 414 applies.

10 Sec. 404. A trustee shall allocate to principal all of the
11 following:

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

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

20 (c) Amounts recovered from third parties to reimburse the
21 trust because of disbursements described in section 502(1)(g) or
22 for other reasons to the extent not based on the loss of income.

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

27 (e) Net income received in an accounting period during which

1 there is no beneficiary to whom a trustee may or must distribute
2 income.

3 (f) Other receipts as provided in sections 408 to 415 of this
4 article.

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

16 Sec. 406. (1) An amount received as interest, whether
17 determined at a fixed, variable, or floating rate, on an
18 obligation to pay money to the trustee, including an amount
19 received as consideration for prepaying principal, shall be
20 allocated to income without any provision for amortization of
21 premium.

22 (2) A trustee shall allocate to principal an amount received
23 from the sale, redemption, or other disposition of an obligation
24 to pay money to the trustee more than 1 year after it is
25 purchased or acquired by the trustee, including an obligation
26 whose purchase price or value when it is acquired is less than
27 its value at maturity. If the obligation matures within 1 year

1 after it is purchased or acquired by the trustee, an amount
2 received in excess of its purchase price or its value when
3 acquired by the trust must be allocated to income.

4 (3) This section does not apply to an obligation to which
5 section 409, 410, 411, 412, 414, or 415 applies.

6 Sec. 407. (1) Except as otherwise provided in subsection
7 (2), a trustee shall allocate to principal the proceeds of a life
8 insurance policy or other contract in which the trust or its
9 trustee is named as beneficiary, including a contract that
10 insures the trust or its trustee against loss for damage to,
11 destruction of, or loss of title to a trust asset. The trustee
12 shall allocate dividends on an insurance policy to income if the
13 premiums on the policy are paid from income and to principal if
14 the premiums are paid from principal.

15 (2) A trustee shall allocate to income proceeds of a contract
16 that insures the trustee against loss of occupancy or other use
17 by an income beneficiary, loss of income, or, subject to section
18 403, loss of profits from a business.

19 (3) This section does not apply to a payment to which section
20 409 applies.

21 Sec. 408. If a trustee determines that an allocation
22 between principal and income required by section 409, 410, 411,
23 412, or 415 is insubstantial, the trustee may allocate the entire
24 amount to principal unless 1 or more of the circumstances
25 described in section 104(4) apply to the allocation. This power
26 may be exercised by a cotrustee in the circumstances described in
27 section 104(5) and may be released for the reasons and in the

1 manner described in section 104(6). An allocation is presumed to
2 be insubstantial if 1 or more of the following apply:

3 (a) The amount of the allocation would increase or decrease
4 net income in an accounting period, as determined before the
5 allocation, by less than 10%.

6 (b) The value of the asset producing the receipt for which
7 the allocation would be made is less than 10% of the total value
8 of the trust's assets at the beginning of the accounting period.

9 Sec. 409. (1) As used in this section, "payment" means a
10 payment that a trustee may receive over a fixed number of years
11 or during the life of 1 or more individuals because of services
12 rendered or property transferred to the payer in exchange for
13 future payments. The term includes a payment made in money or
14 property from the payer's general assets or from a separate fund
15 created by the payer, including a private or commercial annuity,
16 an individual retirement account, or a pension, profit-sharing,
17 stock-bonus, or stock-ownership plan.

18 (2) To the extent that a payment is characterized as interest
19 or a dividend or a payment made in lieu of interest or a
20 dividend, a trustee shall allocate it to income. The trustee
21 shall allocate to principal the balance of the payment and any
22 other payment received in the same accounting period that is not
23 characterized as interest, a dividend, or an equivalent payment.

24 (3) If no part of a payment is characterized as interest, a
25 dividend, or an equivalent payment, and all or part of the
26 payment is required to be made, a trustee shall allocate to
27 income 10% of the part that is required to be made during the

1 accounting period and the balance to principal. If no part of a
2 payment is required to be made or the payment received is the
3 entire amount to which the trustee is entitled, the trustee shall
4 allocate the entire payment to principal. For purposes of this
5 subsection, a payment is not required to be made to the extent
6 that it is made because the trustee exercises a right of
7 withdrawal.

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

13 (5) This section does not apply to payments to which section
14 410 applies.

15 Sec. 410. (1) As used in this section, "liquidating asset"
16 means an asset whose value will diminish or terminate because the
17 asset is expected to produce receipts for a period of limited
18 duration. Liquidating asset includes a leasehold, patent,
19 copyright, royalty right, and right to receive payments during a
20 period of more than 1 year under an arrangement that does not
21 provide for the payment of interest on the unpaid balance.
22 Liquidating asset does not include a payment subject to section
23 409, natural resources subject to section 411, timber subject to
24 section 412, an activity subject to section 414, an asset subject
25 to section 415, or an asset for which the trustee establishes a
26 reserve for depreciation under section 503.

27 (2) A trustee shall allocate to income 10% of the receipts

1 from a liquidating asset and the balance to principal.

2 Sec. 411. (1) Except as provided in subsection (4), to the
3 extent that a trustee accounts for receipts from an interest in
4 minerals or other natural resources pursuant to this section, the
5 trustee shall allocate them as follows:

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

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

12 (c) If an amount received as a royalty, shut-in-well payment,
13 take-or-pay payment, bonus, or delay rental is more than nominal,
14 90% must be allocated to principal and the balance to income.

15 (d) If an amount is received from a working interest or any
16 other interest not provided for in subdivision (a), (b), or (c),
17 90% of the net amount received must be allocated to principal and
18 the balance to income.

19 (2) Except as provided in subsection (4), a trustee shall
20 allocate to income an amount received on account of an interest
21 in water that is renewable. If the interest in water is not
22 renewable, the trustee shall allocate 90% of the amount to
23 principal and the balance to income.

24 (3) This act applies whether or not a decedent or donor was
25 extracting minerals, water, or other natural resources before the
26 interest became subject to the trust.

27 (4) If a trust owns an interest in minerals, water, or other

1 natural resources on the effective date of this act, the trustee
2 may allocate receipts from the interest as provided in this act
3 or in the manner used by the trustee before the effective date of
4 this act. If the trust acquires an interest in minerals, water,
5 or other natural resources after the effective date of this act,
6 the trustee shall allocate receipts from the interest as provided
7 in this act.

8 Sec. 412. (1) Except as provided in subsection (4), to the
9 extent that a trustee accounts for receipts from the sale of
10 timber and related products pursuant to this section, the trustee
11 shall allocate the net receipts as follows:

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

16 (b) To principal to the extent that the amount of timber
17 removed from the land exceeds the rate of growth of the timber or
18 the net receipts are from the sale of standing timber.

19 (c) To or between income and principal if the net receipts
20 are from the lease of timberland or from a contract to cut timber
21 from land owned by a trust, by determining the amount of timber
22 removed from the land under the lease or contract and applying
23 the rules in subdivisions (a) and (b).

24 (d) To principal to the extent that advance payments,
25 bonuses, and other payments are not allocated pursuant to
26 subdivision (a), (b), or (c).

27 (2) In determining net receipts to be allocated pursuant to

1 subsection (1), a trustee may deduct and transfer to principal a
2 reasonable amount for depletion.

3 (3) This act applies whether or not a decedent or transferor
4 was harvesting timber from the property before it became subject
5 to the trust.

6 (4) If a trust owns an interest in timberland on the
7 effective date of this act, the trustee may allocate net receipts
8 from the sale of timber and related products as provided in this
9 act or in the manner used by the trustee before the effective
10 date of this act. If the trust acquires an interest in
11 timberland after the effective date of this act, the trustee
12 shall allocate net receipts from the sale of timber and related
13 products as provided in this act.

14 Sec. 413. (1) If a marital deduction is allowed for all or
15 part of a trust whose assets consist substantially of property
16 that does not provide the spouse with sufficient income from or
17 use of the trust assets, and if the amounts that the trustee
18 transfers from principal to income under section 104 and
19 distributes to the spouse from principal pursuant to the terms of
20 the trust are insufficient to provide the spouse with the
21 beneficial enjoyment required to obtain the marital deduction,
22 the spouse may require the trustee to make property productive of
23 income, convert property within a reasonable time, or exercise
24 the power conferred by section 104(1). The trustee may decide
25 which action or combination of actions to take.

26 (2) In cases not governed by subsection (1), proceeds from
27 the sale or other disposition of an asset are principal without

1 regard to the amount of income the asset produces during any
2 accounting period.

3 Sec. 414. (1) As used in this section, "derivative" means a
4 contract or financial instrument or a combination of contracts
5 and financial instruments that gives a trust the right or
6 obligation to participate in some or all changes in the price of
7 a tangible or intangible asset or group of assets, or changes in
8 a rate, an index of prices or rates, or other market indicator
9 for an asset or a group of assets.

10 (2) To the extent that a trustee accounts for transactions in
11 derivatives under this section, the trustee shall allocate to
12 principal receipts from and disbursements made in connection with
13 those transactions.

14 (3) If a trustee grants an option to buy property from the
15 trust, whether or not the trust owns the property when the option
16 is granted, grants an option that permits another person to sell
17 property to the trust, or acquires an option to buy property for
18 the trust or an option to sell an asset owned by the trust, and
19 the trustee or other owner of the asset is required to deliver
20 the asset if the option is exercised, an amount received for
21 granting the option must be allocated to principal. An amount
22 paid to acquire the option must be paid from principal. A gain
23 or loss realized upon the exercise of an option, including an
24 option granted to a settlor of the trust for services rendered,
25 must be allocated to principal.

26 Sec. 415. (1) As used in this section, "asset-backed
27 security" means an asset whose value is based upon the right it

1 gives the owner to receive distributions from the proceeds of
2 financial assets that provide collateral for the security.
3 Asset-backed security includes an asset that gives the owner the
4 right to receive from the collateral financial assets only the
5 interest or other current return or only the proceeds other than
6 interest or current return. Asset-backed security does not
7 include an asset to which section 401 or 409 applies.

8 (2) If a trust receives a payment from interest or other
9 current return and from other proceeds of the collateral
10 financial assets of an asset-backed security, the trustee shall
11 allocate to income the portion of the payment that the payer
12 identifies as being from interest or other current return and
13 shall allocate the balance of the payment to principal.

14 (3) If a trust receives 1 or more payments in exchange for
15 the trust's entire interest in an asset-backed security in 1
16 accounting period, the trustee shall allocate the payments to
17 principal. If a payment is 1 of a series of payments that will
18 result in the liquidation of the trust's interest in the security
19 over more than 1 accounting period, the trustee shall allocate
20 10% of the payment to income and the balance to principal.

21 ARTICLE 5

22 Sec. 501. A trustee shall make the following disbursements
23 from income to the extent that they are not disbursements to
24 which section 201(b)(ii) or (iii) applies:

25 (a) One-half of the regular compensation of the trustee and
26 of any person providing investment advisory or custodial services
27 to the trustee.

1 (b) One-half of all expenses for accountings, judicial
2 proceedings, or other matters that involve both the income and
3 remainder interests.

4 (c) All of the other ordinary expenses incurred in connection
5 with the administration, management, or preservation of trust
6 property and the distribution of income, including interest,
7 ordinary repairs, regularly recurring taxes assessed against
8 principal, and expenses of a proceeding or other matter that
9 concerns primarily the income interest.

10 (d) Recurring premiums on insurance covering the loss of a
11 principal asset or the loss of income from or use of the asset.

12 Sec. 502. (1) A trustee shall make the following
13 disbursements from principal:

14 (a) The remaining 1/2 of the disbursements described in
15 section 501(a) and (b).

16 (b) All of the trustee's compensation calculated on principal
17 as a fee for acceptance, distribution, or termination, and
18 disbursements made to prepare property for sale.

19 (c) Payments on the principal of a trust debt.

20 (d) Expenses of a proceeding that concerns primarily
21 principal, including a proceeding to construe the trust or to
22 protect the trust or its property.

23 (e) Premiums paid on a policy of insurance not described in
24 section 501(d) of which the trust is the owner and beneficiary.

25 (f) Estate, inheritance, and other transfer taxes, including
26 penalties, apportioned to the trust.

27 (g) Disbursements related to environmental matters, including

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

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

15 Sec. 503. (1) As used in this section, "depreciation" means
16 a reduction in value due to wear, tear, decay, corrosion, or
17 gradual obsolescence of a fixed asset having a useful life of
18 more than 1 year.

19 (2) A trustee may transfer to principal a reasonable amount
20 of the net cash receipts from a principal asset that is subject
21 to depreciation, but may not transfer an amount for depreciation
22 as follows:

23 (a) An amount for that portion of real property used or
24 available for use by a beneficiary as a residence or an amount
25 for tangible personal property held or made available for the
26 personal use or enjoyment of a beneficiary.

27 (b) An amount during the administration of a decedent's

1 estate.

2 (c) An amount under this section, if the trustee is
3 accounting under section 403 for the business or other activity
4 in which the asset is used.

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

7 Sec. 504. (1) If a trustee makes or expects to make a
8 principal disbursement described in this section, the trustee may
9 transfer an appropriate amount from income to principal in 1 or
10 more accounting periods to reimburse principal or to provide a
11 reserve for future principal disbursements.

12 (2) Principal disbursements to which subsection (1) applies
13 include the following, but only to the extent that the trustee
14 has not been and does not expect to be reimbursed by a third
15 party:

16 (a) An amount chargeable to income but paid from principal
17 because it is unusually large, including extraordinary repairs.

18 (b) A capital improvement to a principal asset, whether in
19 the form of changes to an existing asset or the construction of a
20 new asset, including special assessments.

21 (c) Disbursements made to prepare property for rental,
22 including tenant allowances, leasehold improvements, and broker's
23 commissions.

24 (d) Periodic payments on an obligation secured by a principal
25 asset to the extent that the amount transferred from income to
26 principal for depreciation is less than the periodic payments.

27 (e) Disbursements described in section 502(1)(g).

1 (3) If the asset whose ownership gives rights to the
2 disbursements becomes subject to a successive income interest
3 after an income interest ends, a trustee may continue to transfer
4 amounts from income to principal as provided in subsection (1).

5 Sec. 505. (1) A tax required to be paid by a trustee based
6 on receipts allocated to income shall be paid from income.

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

10 (3) A tax required to be paid by a trustee on the trust's
11 share of an entity's taxable income must be paid proportionately
12 as follows:

13 (a) From income to the extent that receipts from the entity
14 are allocated to income.

15 (b) From principal to the extent that:

16 (i) Receipts from the entity are allocated to principal.

17 (ii) The trust's share of the entity's taxable income exceeds
18 the total receipts described in subdivision (a) and subparagraph
19 (i).

20 (4) For purposes of this section, receipts allocated to
21 principal or income must be reduced by the amount distributed to
22 a beneficiary from principal or income for which the trust
23 receives a deduction in calculating the tax.

24 Sec. 506. (1) A fiduciary may make adjustments between
25 principal and income to offset the shifting of economic interests
26 or tax benefits between income beneficiaries and remainder
27 beneficiaries that arise from 1 or more of the following:

1 (a) Elections and decisions, other than those described in
2 subsection (2), that the fiduciary makes from time to time
3 regarding tax matters.

4 (b) An income tax or any other tax that is imposed upon the
5 fiduciary or a beneficiary as a result of a transaction involving
6 or a distribution from the estate or trust.

7 (c) The ownership by an estate or trust of an interest in an
8 entity whose taxable income, whether or not distributed, is
9 includable in the taxable income of the estate, trust, or a
10 beneficiary.

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

27

ARTICLE 6

House Bill No. 5307 as amended February 3, 2004

1 Sec. 601. In applying and construing this act,
2 consideration shall be given to the need to promote uniformity of
3 the law with respect to the subject matter of this act among
4 states that enact it.

5 Sec. 602. If any provision of this act or its application
6 to any person or circumstance is held invalid, the invalidity
7 does not affect other provisions or applications of this act that
8 can be given effect without the invalid provision or application,
9 and to this end the provisions of this act are severable.

10 Sec. 603. [The revised uniform principal and income act, 1965 PA
11 340, MCL 555.51 to 555.68, is repealed.

12

13]

14 Sec. 604. [This act takes effect May 1, 2004.

15

 Sec. 605. This act applies to each trust or descendant's estate
existing on the effective date of this act except as otherwise expressly
provided in the will or terms of the trust or in this act.]