

**HOUSE OF REPRESENTATIVES STAFF ANALYSIS**

**BILL #:** HB 1755                      Trusts  
**SPONSOR(S):** Committee on Judiciary and Rep. Kottkamp  
**TIED BILLS:**    **IDEN./SIM. BILLS:**

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REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Judiciary	17 Y, 0 N	Thomas	Havlicak
2)			
3)			
4)			
5)			

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**SUMMARY ANALYSIS**

The bill addresses three separate areas related to the administration of trusts: expansion of the Uniform Transfer-on-Death Security Registration Act to bank and trust company investments; clarification to the payment of trustee's costs and attorney's fees; and technical corrections to the Uniform Principal and Income Act (UPIA). The UPIA is codified at Ch. 738, F.S., and governs the identification, allocation, and apportionment of assets between principal and income in or from a trust property through a trust instrument, will, or other governing instrument. In 2002, the Legislature substantially revised ch. 738, F.S., by enacting Florida's UPIA. Last year, the Legislature adopted further revisions to ch. 738, F.S., making technical and clarifying changes to the UPIA.

The bill does not appear to have a fiscal impact on state or local government.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. DOES THE BILL:

- |                                      |                              |                             |   |
|--------------------------------------|------------------------------|-----------------------------|---|
| 1. Reduce government?                | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 2. Lower taxes?                      | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 3. Expand individual freedom?        | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 4. Increase personal responsibility? | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |
| 5. Empower families?                 | Yes <input type="checkbox"/> | No <input type="checkbox"/> | N/A <input checked="" type="checkbox"/> |

For any principle that received a “no” above, please explain:

#### B. EFFECT OF PROPOSED CHANGES:

The bill addresses three separate areas related to the administration of trusts: expansion of the Uniform Transfer-on-Death Security Registration Act to bank and trust company investments; clarification to the payment of trustee’s costs and attorney’s fees; and technical corrections to the Uniform Principal and Income Act (UPIA). The UPIA is codified at Ch. 738, F.S., and governs the identification, allocation, and apportionment of assets between principal and income in or from a trust property through a trust instrument, will, or other governing instrument. In 2002, the Legislature substantially revised ch. 738, F.S., by enacting Florida’s UPIA. Last year, the Legislature adopted further revisions to ch. 738, F.S., making technical and clarifying changes to the UPIA.

#### Trusts

There are several different forms of trusts, and numerous types of property held by trusts. The trustee of a trust and the personal representative of a decedent's estate are considered fiduciaries.<sup>1</sup> The trustee has a fiduciary duty toward the beneficiaries of the trust to manage the trust properly to satisfy both the interests of the trust's income beneficiaries during the life of the trust and the interests of the remainder beneficiaries at the trust's termination.<sup>2</sup>

A trustee’s management of any trust involves an inherent conflict between the interests of current beneficiaries and future beneficiaries. The current beneficiaries seek the largest possible payout given to them from the trust, while the future beneficiaries seek the minimum possible payout to present beneficiaries in order to maximize the amount that the future beneficiary will receive. Determining the proper balance between current beneficiaries and future beneficiaries necessarily entails difficult policy considerations. The grantor of a trust generally provides a distribution plan within the trust document that the grantor deems appropriate. There are many situations, however, where the terms of a trust do not clearly specify how the distribution of the trust assets is to be made.

#### **Section 1 – Expansion of the Uniform Transfer-on-Death Security Registration Act to Bank and Trust Company Investments**

Chapter 711, F.S., regulates the registration of securities in beneficiary form.<sup>3</sup> The provisions of this chapter provide for the ability to register securities in joint security accounts and other types of security accounts with a survivorship feature.<sup>4</sup> A security account is defined as:

<sup>1</sup> Section 738.102(3), F.S.

<sup>2</sup> Section 738.103, F.S.

<sup>3</sup> Chapter 711, F.S., is known as the “Uniform Transfer-on-Death Security Registration Act” pursuant to s. 711.50, F.S.

- (a) A reinvestment account associated with a security, a securities account with a broker, a cash balance in a brokerage account, cash, interest, earnings, or dividends earned or declared on a security in an account, a reinvestment account, or a brokerage account, whether or not credited to the account before the owner's death; or
- (b) A cash balance or other property held for or due to the owner of a security as a replacement for or product of an account security, whether or not credited to the account before the owner's death.<sup>5</sup>

The provisions of ch. 711, F.S., do not apply to accounts within investment agencies, banks, or trust companies. It has been claimed that the present law “gives brokerage accounts an unfair benefit without good reason to exclude banks and trust companies. Other states have revised their version of the Act to include investment agency accounts at bank trust departments. Banks and trust companies can greatly benefit from having the opportunity to open accounts that include transfer on death benefits.”<sup>6</sup>

### Proposed Changes

Section 1 of the bill expands the definition of “security account” to make the provisions of ch. 711, F.S., relating to the registration of securities in beneficiary form applicable to security accounts within investment agencies, banks, and trust companies.

### **Sections 2 and 3 – Clarification to the Payment Of Trustee’s Costs And Attorney’s Fees**

Trustees often may be involved in legal proceedings relating to the trusts which they serve. When legal proceedings are instituted, trustees are required to retain and pay legal counsel. Florida courts have broad supervisory authority over the payment of costs and attorney fees in connection with these trust proceedings.<sup>7</sup> Courts may order a party to pay another party's costs and attorney's fees.<sup>8</sup> Courts may order the reimbursement of excessive fees paid to attorneys by a trust.<sup>9</sup>

The Fourth District Court of Appeals, based on its interpretation of s. 737.403(2), F.S.,<sup>10</sup> ruled in a case involving a breach of trust allegation against the trustee, that a conflict of interest is present and a trustee cannot pay its costs and attorney's fees from trust assets without prior court approval.<sup>11</sup> The Court indicated that the trustee should have obtained Court approval prior to paying attorney fees from the assets of the trust even though payment from trust assets came after the breach of trust allegation was resolved by the Court in favor of the trustee.<sup>12</sup> Based on the Court's ruling, court approval is required in advance for payment of a trustee's costs and attorney's fees from trust assets where the trust proceeding involves an allegation of breach of trust by the trustee. In situations where advance

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<sup>4</sup> A “security” is defined “as a share, participation, or other interest in property, in a business, or in an obligation of an enterprise or other issuer, and includes a certificated security, an uncertificated security, and a security account.” See section 711.501(9), F.S.

<sup>5</sup> Section 711.501(10), F.S.

<sup>6</sup> Florida Bankers Association, Florida Institute of Certified Public Accountants, and the Real Property, Probate and Trust Law Section of the Florida Bar, *White Paper: Expansion of Uniform Transfer on Death Security Registration Act to Trust Company Investments*, October 1, 2003 (on file with the House Committee on Judiciary).

<sup>7</sup> Section 737.2035, F.S.

<sup>8</sup> Section 737.4033, F.S.

<sup>9</sup> Section 737.204(3), F.S.

<sup>10</sup> Section 737.403(2), F.S., reads: “(2) If the duty of the trustee and the trustee's individual interest or his or her interest as trustee of another trust conflict in the exercise of a trust power, the power may be exercised only by court authorization, except as provided in s. 737.402(2)(a), (e), (g), (s) and (y). Under this section, personal profit or advantage to an affiliated or subsidiary company or association is personal profit to any corporate trustee.”

<sup>11</sup> *Shriner v. Dyer*, 462 So.2d 1122 (Fla. 4<sup>th</sup> DCA 1984).

<sup>12</sup> *Id.* at 1124.

approval is not required, it is the customary practice of trustees to pay their costs and attorney's fees from assets of the trust unless a contrary order is imposed by the court.

It has been reported that “[m]ost trust proceedings are resolved through settlement or other means that do not involve a contested hearing or trial. It is unreasonable to require trustees to seek prior court approval to pay costs and attorney’s fees from trust assets in all cases merely because there has been a breach of trust allegation at some point in the proceeding. The better approach is to require a trustee to seek prior court approval only when the breach of trust allegation is pending. Once resolved, the trustee can pay fees from trust assets unless the court has ordered the trustee to bear its own costs and attorney’s fees, or unless the breach of trust has been established.”<sup>13</sup>

### Proposed Changes

Section 2 of the bill amends s. 737.402, F.S., to authorize a trustee, unless otherwise provided in the trust agreement, to pay compensation and costs incurred in connection with the retention of legal counsel from the assets of the trust to advise the trustee in the exercise of the trustee’s powers and to represent the trustee in legal proceedings, including appeals.

Section 3 of the bill amends s. 737.403, F.S., to provide that court authorization is not required to permit deviations or to approve transactions involving a conflict of interest in the following situations:

- The exercise of any power described in s. 737.402(2)(a), (e), (g), (s) or (y);<sup>14</sup>
- The exercise of any power for which the trust instrument acknowledges the trustee’s conflict of interest and expressly authorizes the exercise of that power notwithstanding the conflict;
- The exercise of any power consented to in writing by a settlor of the trust while the settlor holds the right of revocation of the trust;
- The exercise of any power consented to in writing by each of the beneficiaries to whom the trustee is required to provide any annual or periodic accounting; or
- Payment of costs or attorney’s fees incurred in any trust proceeding.

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<sup>13</sup> Florida Bankers Association, Florida Institute of Certified Public Accountants, and the Real Property, Probate and Trust Law Section of the Florida Bar, *White Paper: Trustee’s Costs and Attorney’s Fees*, November 19, 2003 (on file with the House Committee on Judiciary).

<sup>14</sup> These subsections read as follows:

737.402 Powers of trustees conferred by this part.--

(2) Unless otherwise provided in the trust instrument, a trustee has the power:

(a) To collect, hold, and retain trust assets received from a settlor until disposition of the assets should be made. The assets may be retained even though they include an asset in which the trustee is personally interested.

(e) To acquire an undivided interest in a trust asset, including, but not limited to, a money market mutual fund, mutual fund, or common trust fund, in which asset the trustee holds an undivided interest in any trust capacity, including any money market or other mutual fund from which the trustee, any cotrustee, or any affiliate or associate of the trustee or cotrustee is entitled to receive reasonable compensation for providing necessary services as an investment adviser, portfolio manager, or servicing agent. A trustee, cotrustee, or affiliate or associate of the trustee or cotrustee may receive compensation for such services in addition to fees received for administering the trust, provided such compensation is fully disclosed in writing to all current income beneficiaries of the trust.

(g) If a bank, to deposit trust funds in another department of the same entity or in a bank that is affiliated with the trustee bank.

(s) To borrow money to be repaid from trust assets or otherwise, and to advance money for the protection of the trust and for all expenses, losses, and liabilities sustained in the administration of the trust or because of the holding or ownership of any trust assets, for which advances, with any interest, the trustee has a lien on the trust assets as against the beneficiary.

(y) To employ persons, including attorneys, auditors, investment advisers, or agents, even if they are the trustee or associated with the trustee, to advise or assist the trustee in the performance of his or her administrative duties; to act without independent investigation upon their recommendations; and, instead of acting personally, to employ one or more agents to perform any act of administration, whether or not discretionary.

## **Sections 4, 5, and 6: Technical Revisions to the Uniform Principal and Income Act (UPIA)**

### **Florida Uniform Principal and Income Act**

Chapter 738, F.S., governs the identification of principal and income in or from a trust property through a trust instrument, will, or other governing instrument; the allocation of principal and income; and the apportionment of assets between income and principal. In 2002, the Legislature substantially revised ch. 738, F.S., by enacting Florida's Uniform Principal And Income Act (UPIA).<sup>15</sup> The UPIA made sweeping changes to Florida's principal and income laws. Last year, the Legislature adopted further revisions to ch. 738, F.S., making necessary technical and clarifying changes to the UPIA.<sup>16</sup> The intent of the Act is to:

- Provide more precise procedures for trustees and personal representatives in the administration of a trust or an estate.
- Provide greater specificity as to what constitutes income and principal and the formulas for allocation of assets to principal and income.
- Ensure proper distribution to beneficiaries, heirs, and devisees.
- Reflect changes in principal and allocation rules consistent with modern trust investment principles and practices.

The guiding principle under chapter 738, F.S., is to ensure that the intent of the creator of the trust governs the interpretation and construction of the trust. Therefore, the default rules of chapter 738, F.S., are only operative in the event a trust document, will, or other governing instrument is silent. Additional technical and clarifying changes have been identified by interested industry groups that were proponents of the UPIA.<sup>17</sup> These technical and clarifying issues are as follows:

#### **Issue I**

Section 738.104(3)(h), F.S., prohibits a trustee from making an adjustment to a trust if the adjustment would benefit the trustee directly or indirectly. Trustees who are paid an annual fee based upon the value of trust assets arguably benefit indirectly by adjustments to assets from income to principle.

The proposed change in section 4 of the bill amends s. 738.104(3)(h), F.S., to provide that it is not a conflict of interest for a trustee whose compensation is based on the value of the trust to make adjustments which affect the value of the trust.

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<sup>15</sup> Chapter 2002-42, L.O.F. This Act is based upon the Uniform Principal and Income Act (1997) promulgated by the National Conference of Commissioners on Uniform State Laws (NCCUSL). Florida's Act also includes a number of provisions not found in the NCCUSL version of the uniform act.

<sup>16</sup> Chapter 2003-43, L.O.F.

<sup>17</sup> Florida Bankers Association, Florida Institute of Certified Public Accountants, and the Real Property, Probate and Trust Law Section of the Florida Bar, *White Paper: Uniform Principal and Income Act Technical Corrections*, December 10, 2003 (on file with the House Committee on Judiciary).

## **Issue II**

Section 738.1041(12), F.S., states that the section "shall be construed as pertaining to the administration of a trust." Similar language should be included in s. 738.104, F.S., to make it clear that when administration of a trust is governed by Florida law, but the substantive provisions are governed by the laws of another state, that adjustments under s. 738.104, F.S., are to be considered administrative.

The proposed change in section 4 of the bill creates a new subsection (11) to s. 738.104, F.S., to provide that the section pertains to the administration of trusts and is available for any trust administered under the laws of Florida.

## **Issue III**

Section 738.1041, F.S., provides for the regulation of total return unitrusts.<sup>18</sup> This section uses the term "fair market value" throughout, however, the term is not defined. This section also uses the term "unitrust amount," however, this term is not defined. Other terms are defined in subsection (1).

The proposed change in section 5 of the bill amends section 738.1041(1), F.S., to provide a definition of "fair market value" and a definition of "unitrust amount."

## **Issue IV**

Section 738.105(3), F.S., provides trustees with protection from liability under certain circumstances and provides a remedy when a trustee is found to have abused its discretion. The remedy is to restore the income and remainder beneficiaries to the positions they would have occupied had the trustee not abused its discretion.<sup>19</sup> It is unclear whether these provisions apply to a trustee who submits or fails to submit a unitrust plan or modification to a unitrust plan.

The proposed change in section 5 of the bill amends s. 738.1041(10), F.S., to specifically make applicable the provisions of s. 738.105(3), F.S., to trustees over unitrusts.

## **Issue V**

Often the "administration" of a trust is governed by the law of one state and the "rights of beneficiaries, construction and validity" are governed by the law of a different state.<sup>20</sup> Section 738.1041(12), F.S., states that the section "shall be construed as pertaining to the administration of a trust and shall be available to any trust that is administered in this state under Florida law..." The option should not be limited to trusts administered in Florida but should be available to all trusts, the administration of which is governed by Florida law.

The proposed change in section 5 of the bill amends s. 738.1041(12), F.S., to provide that the unitrust election is available for any trust administered under the laws of Florida.

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<sup>18</sup> While the provisions of s. 738.1041, F.S., address the regulation of total return unitrusts (TRU) in Florida, the term "total return unitrust" is not defined in statute. A TRU is a financial and estate planning tool which pays the current income beneficiary a fixed percentage based on the value of the trust. This frees the trustee to manage the trust based on total return on the investments, whether it benefits income or principle.

<sup>19</sup> Section 738.105(3), F.S.

<sup>20</sup> See, George Gleason Bogert, *The Law of Trusts and Trustees* §§ 293, 297, and 861 [2d ed. (rev.) 1992].

## Issue VI

Section 738.301(4), F.S., states "an income interest ends on the day before an income beneficiary dies . . .". Section 738.303(1), F.S., states that undistributed income is net income received "before the date on which an income interest ends." Since an income interest ends the day before the income beneficiary dies, and undistributed income is only income received before the date the income interest ends (e.g. before the day before the death of the beneficiary), then technically undistributed income is only that income received 2 days before the income beneficiary dies. As presently written, there is confusion over income received the day before the beneficiary's death.

The proposed change in section 6 of the bill amends s. 738.303(1), F.S., to define "undistributed income" as income earned on or before the day that the income interest ends. In the case of a unitrust, the term will mean the daily pro-rated unitrust amount ending on the day the income interest ends.

### C. SECTION DIRECTORY:

**Section 1:** Amends s. 711.501, F.S., relating to the definition of "security account."

**Section 2:** Amends s. 737.402, F.S., relating to the powers of trustees.

**Section 3:** Amends s. 737.403, F.S., relating to the power of courts to permit deviations or to approve transactions involving a conflict of interest.

**Section 4:** Amends s. 738.104, F.S., relating to a trustee's power to make adjustments.

**Section 5:** Amends s. 738.1041, F.S., relating to total return unitrusts.

**Section 6:** Amends s. 738.303, F.S., relating to the definition of "undistributed income" for purposes of apportionment when income ends.

**Section 7:** Provides that the bill takes effect upon becoming a law.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

### A. FISCAL IMPACT ON STATE GOVERNMENT:

#### 1. Revenues:

The bill does not appear to have any impact on state revenues.

#### 2. Expenditures:

The bill does not appear to have any impact on state expenditures.

### B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

#### 1. Revenues:

The bill does not appear to have any impact on local governments' revenues.

#### 2. Expenditures:

The bill does not appear to have any impact on local governments' expenditures.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The ability to take advantage of more flexible trust provisions could result in more equitable trust distributions and better tax situations for trust beneficiaries. It has been claimed that the present law as provided under ch. 711, F.S., related to uniform transfer-on-death security registration "gives brokerage accounts an unfair benefit without good reason to exclude banks and trust companies. Other states have revised their version of the Act to include investment agency accounts at bank trust departments. Banks and trust companies can greatly benefit from having the opportunity to open accounts that include transfer on death benefits."<sup>21</sup>

D. FISCAL COMMENTS:

None.

**III. COMMENTS**

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable because this bill does not appear to require counties or cities to: spend funds or take action requiring the expenditure of funds; reduce the authority of counties or cities to raises revenues in the aggregate; or reduce the percentage of a state tax shared with counties or cities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

The bill does not create the need for rulemaking authority.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

**IV. AMENDMENTS/COMMITTEE SUBSTITUTE CHANGES**

N/A

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<sup>21</sup> Florida Bankers Association, Florida Institute of Certified Public Accountants, and the Real Property, Probate and Trust Law Section of the Florida Bar, *White Paper: Expansion of Uniform Transfer on Death Security Registration Act to Trust Company Investments*, October 1, 2003 (on file with the House Committee on Judiciary).