

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 2926

SPONSOR: Banking and Insurance Committee and Senator Atwater

SUBJECT: Trusts and Other Agency Relationships

DATE: March 31, 2004

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Knudson</u>	<u>Deffenbaugh</u>	<u>BI</u>	<u>Fav/CS</u>
2.	_____	_____	<u>JU</u>	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____
6.	_____	_____	_____	_____

I. Summary:

Committee Substitute for Senate Bill 2926 amends the Florida Uniform Transfer-on-Death Security Registration Act (ch. 711, F.S.) to allow banks and trust companies to open accounts that include transfer on death benefits by amending the definition of “security account.”

The bill makes changes to the powers of trustees under part IV of ch. 737, F.S. The bill specifies that a trustee has the authority to use trust assets to pay compensation and costs incurred in connection with employing attorneys, auditors, investment advisers or agents to assist the trustee in performing his or her administrative duties. The bill also states that trust assets may be used to prosecute or defend a legal action and to pay compensation and costs to attorneys and other agents that assist the trustee in doing so. The bill adds “appeals” to the legal proceedings covered under this authority.

This bill amends various provisions of the 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. The bill makes primarily technical and clarifying changes, as follows:

- The bill provides four situations for which a trustee does not need court authorization to exercise power.
- The bill provides an exception to the rule that the trustee may not make an adjustment if the adjustment would benefit the trustee. Under the bill, a trustee may make an adjustment if the trustee’s compensation is based upon the value of trust assets.
- The bill defines the terms “fair market value” and “unitrust amount,” and amends the definition of “undistributed income.”

- The bill provides that if a trustee or disinterested person does not act in good faith, the provisions of s. 738.105(3), F.S., apply. Thus, if a trustee of a unitrust does not act in good faith in submitting or failing to submit a unitrust plan or modification, a court will have authority to correct the trustee's actions.
- The bill makes it clear that when the administration of a trust is governed by Florida law, but the substantive provisions are governed by the laws of another state, adjustments under s. 738.104, F.S., are administrative and thus governed by Florida law.

This bill substantially amends the following sections of the Florida Statutes: 711.501, 737.402, 737.403, 738.104, 738.1041, and 738.303.

II. Present Situation:

Chapter 711, F.S., contains the Florida Uniform Transfer on Death Security Registration Act, the purpose of which is to provide a uniform means by which securities may be registered in beneficiary form. It enables the owner of a security to devise ownership of the security to another party upon the owner's death. Securities may be registered in various types of accounts, including joint accounts with a survivorship feature.

Part IV of ch. 737, F.S., enumerates the powers that a trustee has in administering a trust. Trustees are given various powers, including the collection, retention and distribution of assets from a settlor (the creator of the trust). The trustee may also reinvest trust assets as allowed by the terms of the trust or provided by law, and take a variety of actions as permitted in the trust instrument or by law.

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. The Florida Legislature enacted the Florida Uniform Principal and Income Act during the 2002 legislative session.¹ The legislation substantially revised ch. 738, F.S. by repealing the existing provisions of ch. 738, F.S., and enacting the Uniform Principal and Income Act, as modified.² The intent of the Act was to:

¹ Chapter 2002-42, L.O.F.

² This Act is based the Uniform Principal and Income Act (1997) promulgated by the National Conference of Commissioners on Uniform State Laws. Florida's Act also includes a number of provisions not found in the NCCUSL version of the uniform act. For example, ch. 738, F.S. provides that: 1) There is no express or implied duty to exercise a power to adjust between principal and income or vice versa (s. 738.104(7), F.S.); 2) Beneficiaries, by a super majority, have a right to object to a trustee's discretionary power to adjust between principal and income (s. 738.104(8), F.S.); 3) A trustee has the discretionary power to convert an income trust to a total return unitrust or reconvert a total return unitrust to an income trust (s.738.1041, F.S.); 4) Value of trust assets is to be determined on an asset-by-asset basis and a challenge to such valuation must be made within 6 months of notice of such valuation (s. 738.202(5), F.S.); 5) State law on the apportionment of estate taxes trumps any apportionment provision in ch. 738, F.S. (s. 738.302(4),F.S.); 6) New shares of stock purchased from reinvested dividends retain their character as income (s. 738.401(4), F.S.); 7) provisions governing the sale and collection of interest from bonds and other obligations to pay were expanded (s. 738.503(3), F.S.); 8) A trustee must allocate to income payments received in the nature of interest or dividends under specified circumstances (s. 738.602(2)(a)2., F.S.); 9) An additional category of expenses for extraordinary repairs or expenses in capital improvements may be charged against the principal (s. 738.702(1)(h), F.S.); 10) The amount of depreciation taken for tax purposes is presumptively the correct depreciation for allocating between principal and income (s. 738.703(3), F.S.); 11) A formula for appointing expenses between a life tenant and the remainder interests is provided. See s. 738.801, F.S. The following provisions were originally found in the Uniform

- Provide more precise procedures for trustees and personal representatives in the administration of a trust or an estate, respectively.
- Specify more clearly 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 ch. 738, F.S., is to ensure that the trust's creator's intent governs the interpretation and construction of the trust or other governing instrument. Therefore, the default rules of ch. 738, F.S., are only operative in the event a trust document, will, or other governing instrument is silent.

III. Effect of Proposed Changes:

Section 1. Amends s. 711.501(10), F.S., to amend the definition of "security account," thereby allowing banks and trust companies to open accounts that include transfer on death benefits. Under the bill, a "security account" includes an investment management, investment advisory, investment agency, custody, or other account with a bank or trust company, including the securities in the account, the cash balance, all cash equivalents, and interest, earnings, or dividends earned or declared on a security in the account, whether or not credited to the account before the owner's death. The purpose of the change is to include investment accounts at banks and trust companies within the definition of "security account." The current definition gives an unfair advantage to brokerage accounts, and proponents of the bill state there is no good reason to exclude banks and trust companies, which could benefit from the ability to open accounts that include transfer on death benefits.

Section 2. The bill amends paragraphs (y) and (z) of s. 737.402(2), F.S. The section expands the powers of a trustee to spend trust funds. It specifies that a trustee has the authority to use trust assets to pay compensation and costs incurred in connection with employing attorneys, auditors, investment advisers or agents to assist the trustee in performing his or her administrative duties. The bill also states that trust assets may be used to prosecute or defend a legal action and to pay compensation and costs to attorneys and other agents that assist the trustee in doing so. The bill adds "appeals" to the legal proceedings covered under this authority.

Section 3. Amends s. 737.403(2), F.S., to expand the situations in which a trustee may exercise power without court authorization. Generally, if a trustee's personal interests conflict with an exercise of trust power, the trustee can only exercise that power with court authorization. The bill provides four situations for which a trustee does not need court authorization to exercise power. The first is when the trust document acknowledges the conflict of interest and expressly

Principal and Income Act (1997) but altered in Florida's version of the uniform act: 1) Section 738.503(2), F.S., does not include the provision in the uniform act which provides that the profit on the sale by a trustee of a note maturing within one year must be allocated to income. However, subsection (3) of this section expands upon the provisions regarding the sale of a bond. 2) Section 738.704(2), F.S., does not include the ability of a trustee to "borrow" principal to pay certain expenses chargeable against income, namely extraordinary repairs and capital improvements. Subsection (4) is added to provide that the principal may only be advanced for mortgage payments if necessary to avoid a default.

authorizes the exercise of that power. The trustee may also exercise any power consented to in writing by a settler of the trust while the settler holds a right of revocation for the trust. The third instance when trust power may be exercised is when the exercise of power is consented to in writing by each of the beneficiaries to whom the trustee is required to provide annual or periodic accounting. Consent may be given by a person who represents the beneficiary under s. 731.303, F.S., or the legal or natural guardian of the beneficiary. Finally, a trustee may use trust assets to pay costs or attorney's fees incurred in a trust proceeding without court order unless an action is pending against the trustee for breach of trust, the trustee withdraws or dismisses the case, or if the trustee is found by the court to have committed a breach of trust.

Section 4. Amends s. 738.104, (3)(h), F.S., which enumerates the trustee's power to adjust between principal and income. The bill provides an exception to the rule that the trustee may not make an adjustment if the adjustment would benefit the trustee. Under the bill, a trustee may make an adjustment if the trustee's compensation is based upon the value of trust assets. The bill also creates subsection (11) of s. 738.104, F.S., which states that the section applies to the administration of a trust and is available to any trust administered in this state or under Florida law. This will allow trustees to use the power of adjustment contained in the Uniform Principal and Income Act (UPIA) in trusts administered in Florida, even if the trust is governed by the laws of a state that has not adopted the UPIA.

Section 5. Amends subsections (1), (10), and (12) of s. 738.1041, F.S., the section of Florida law governing total return unitrusts. The term "fair market value" is defined in paragraph (1)(e) as the fair market value of assets held by the trust as otherwise determined under ch. 738, F.S., reduced by all known non-contingent liabilities, except for liabilities that will, upon payment, represent expenses under ss. 738.701 or 738.702, F.S. The term "unitrust amount" is defined in paragraph (1)(f) as being equal to the fair market value of trust assets multiplied by the percentage of the unitrust amount calculated under paragraph (2)(b). The purpose of the definitions is to provide a standard on how to treat liabilities when determining the fair market value of trust assets in a unitrust, thus attracting trust administration business to Florida.

Subsection (10) is amended to provide that if a trustee or disinterested person does not act in good faith, the provisions of s. 738.105(3), F.S., apply. Thus, if a trustee of a unitrust does not act in good faith in submitting or failing to submit a unitrust plan or modification, a court will have authority to correct the trustee's actions in disbursing or failing to disburse trust assets and restore the beneficiaries to the positions they would have been in if the trustee had not abused his or her discretion. The bill also deletes language in subsection (12) to make clear that when the administration of a trust is governed by Florida law, but the substantive provisions are governed by the laws of another state, adjustments under s. 738.104, F.S., are considered to be administrative and thus governed by Florida law. This will allow trustees to use the unitrust provisions contained in Florida's version of the UPIA in trusts that are administered in Florida, even if the trust is governed by the laws of a state that has not adopted similar provisions, thus attracting trust administration business to Florida.

Section 6. Amends s. 738.303(1), F.S., to state that "undistributed income" in a trust includes not only income received before the date on which an income interest ends (the beneficiary dies), but also income received on the date on which an income interest ends. The change corrects a technical problem in the statutes that had the effect of restricting undistributed income to income

received 2 days before the income interest ends. The bill also defines “undistributed income” in a unitrust as being the prorated unitrust amount computed on a daily basis through the date on which the income interest ends.

Section 7. Provides that the act takes effect upon becoming a law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

The bill makes corrections that should make the administration of trusts more efficient and clarifies ambiguous portions of the law, which may have the effect of reducing costs.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.