2020 Regular Session

HOUSE BILL NO. 123

BY REPRESENTATIVE GREGORY MILLER

(On Recommendation of the Louisiana State Law Institute)

TRUSTS: Provides relative to the allocation of receipts and expense to income and principal

AN ACT

To amend and reenact R.S. 9:2141 through 2144, 2145(1), 2146, 2147 through 2154, and 2156(A), (C), and (E), to enact R.S. 9:2151.1, 2151.2, 2156.1, 2156.2, and Subpart F of Part V of Chapter 1 of Code Title II of Code Book III of Title 9 of the Louisiana Revised Statutes of 1950, to be comprised of R.S. 9:2164, and to repeal R.S. 9:2155 and 2157, relative to the administration of trusts; to provide with respect to allocation to income and principal; to provide for the apportionment and allocation of various types of receipts and expenses; to provide for the obligation to pay money; to provide for charges against income and principal; to provide for transfers from income to principal for depreciation; to provide with respect to the payment of income taxes; to provide for underproductive property; to provide for an effective date and applicability; to provide for redesignation; and to provide for related matters.

Be it enacted by the Legislature of Louisiana:

Section 1. R.S. 9:2141 through 2144, 2145(1), 2146, 2147 through 2154, and 2156(A), (C), and (E) are hereby amended and reenacted, and R.S. 9:2151.1, 2151.2, 2156.1, 2156.2, and Subpart F of Part V of Chapter 1 of Code Title II of Code Book III of Title 9 of the Louisiana Revised Statutes of 1950, comprised of R.S. 9:2164, are hereby enacted to read as follows:

§2141. General rule

A trust shall be administered with due regard to the respective interests of the beneficiaries in the allocation of receipts and ~~expenditures~~ expenses.

§2142. Allocation to beneficiaries of income and principal

A trust receipt ~~shall be credited, or an expenditure charged,~~ or expense shall be allocated to income or principal or partly to each:

(1) In accordance with the terms of the trust instrument, including any provision giving the trustee discretion, notwithstanding contrary provisions of this Subpart~~; or~~.

(2) In accordance with the provisions of this Subpart, in the absence of contrary provisions of the trust instrument~~; or~~.

(3) If no rule is provided in the trust instrument or this Subpart, ~~entirely to principal~~ in accordance with what is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal.

Revision Comments - 2020

Prior law provided that a receipt or expense shall be allocated entirely to principal if no provision in the trust instrument or other provision in this Subpart provided otherwise. This revision changes the default rule in an attempt to be fair to both beneficiaries of income and beneficiaries of principal. It is consistent with other provisions in this revision. See, e.g., R.S. 9:2148, 2151, 2152(A)(4), 2153(A), and 2154(A).

§2143. Allocation to beneficiaries of usufruct and naked ownership

A trust is administered with due regard to the respective interests of beneficiaries of usufruct and naked ownership in the allocation of receipts and ~~expenditures if a receipt is credited or an expenditure is charged~~ expenses to the beneficiary of usufruct or the beneficiary of naked ownership or partly to each:

(1) In accordance with the terms of the trust instrument and the law regulating usufruct, notwithstanding contrary provisions of this Subpart~~;~~.

(2) In accordance with the provisions of this Subpart, in the absence of applicable law regulating usufruct and if the trust instrument contains no provisions to the contrary~~;~~.

(3) If neither of the preceding rules applies, in accordance with what is reasonable and equitable in view of the interests of those who are beneficiaries of usufruct as well as those who are beneficiaries of naked ownership~~, and in view of the manner in which men of ordinary prudence, discretion, and intelligence would act in the management of their own affairs~~.

Revision Comments - 2020

This revision modifies the law in part by making minor semantic clarifications and by deleting the "prudent man" rule that existed under prior law because persons of "ordinary prudence, discretion, and intelligence" do not generally consider the interests of successor beneficiaries in managing their own affairs. See, e.g., UPIA (1997) §103, Comment. Trustees, however, should consider the interests of all beneficiaries in discharging their fiduciary obligations.

§2144. Income and principal distinguished

Receipts paid or delivered in return for the use of ~~money or~~ property forming a part of principal are income, unless this ~~Sub-part~~ Subpart expressly provides to the contrary.

Receipts paid or delivered ~~as the~~ in consideration for the sale or other transfer of property forming a part of principal or as the replacement of property forming a part of principal are principal unless this ~~Sub-part~~ Subpart expressly provides to the contrary.

§2145. When right to income arises

The right of an income beneficiary to income from property in trust arises at the time prescribed in the trust instrument, or, if no time is prescribed and the person receiving the right to income is the first income beneficiary to receive a right to income from the property, then:

(1) At the time the property becomes subject to the trust, with respect to property transferred by inter vivos disposition~~;~~.

* * *

§2146. Apportionment of receipts when right to income arises

A. In the administration of property transferred in trust:

(1) Receipts due but not paid when the right of the first income beneficiary to receive income from the property arises shall be treated as accruing when due~~;~~.

CODING: Words in ~~struck through~~ type are deletions from existing law; words underscored are additions.

(2) Receipts in the form of periodic payments, other than ~~corporate distributions to stockholders~~ receipts on account of an interest in a juridical person or from a plan subject to R.S. 9:2151.2, not due when the right of the first income beneficiary to receive income from the property arises, shall be treated as accruing from day to day~~;~~.

(3) Receipts in the form of ~~corporate~~ distributions ~~to stockholders~~ on account of an interest in a juridical person, which are allocated to income under R.S. 9:2149, shall be treated as accruing on the date fixed for the determination of ~~stockholders of record~~ those entitled to distribution, or, if no date is fixed, on the date of declaration of the distribution by the ~~corporation;~~ juridical person.

(4) All other receipts shall be treated as accruing at the time of payment.

B. Receipts treated as accruing after the right of the first income beneficiary to receive income from the property arises, are income if they otherwise are income under the provisions of this ~~Sub-part~~ Subpart. Receipts treated as accruing at an earlier time are principal.

Revision Comments - 2020

This revision is consistent with prior law but expands the law to address receipts from juridical persons other than corporations. According to general principles of civil law, "[a] juridical person is an entity to which the law attributes personality, such as a corporation or a partnership." Civil Code Article 24.

§2147. Apportionment of receipts when right to income ceases

Upon the termination of an income interest, the income beneficiary whose interest is terminated (or his heirs, legatees, or assignees) is entitled to receive any required distributions of or from the following:

(1) Income paid to the trustee but undistributed on the date of termination~~;~~.

(2) Income due but not paid to the trustee on the date of termination~~;~~.

(3) Income in the form of periodic payments subject to daily accrual, other than ~~corporate distributions to stockholders~~ periodic payments on account of an interest in a juridical person, not due on the date of termination~~, accrued from day to day;~~ but accrued prior to the date of termination.

(4) ~~Corporate distributions to stockholders~~ Distributions on account of an interest in a juridical person, which are allocated to income under R.S. 9:2149, paid ~~as income~~ after the termination of the interest if the date for determination of ~~stockholders of record~~ those entitled to distribution is a date before the termination of the interest, or, in the event no date is fixed, if the date of declaration of the distribution by the ~~corporation~~ juridical person is a date before termination of the interest.

Revision Comments - 2020

This revision is consistent with prior law but expands the law to address receipts from juridical persons other than corporations. See Civil Code Article 24.

§2148. Succession receipts

Succession receipts ~~shall be credited~~ and ~~succession expenditures~~ expenses shall be ~~charged~~ allocated to a legacy in trust in accordance with ~~the laws regulating donations mortis causa~~ what is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal.

Revision Comments - 2020

(a) This revision changes the law by no longer deferring to the Civil Code regarding the allocation of receipts and expenses for a legacy in trust.

(b) In many cases, information from a succession representative may be helpful to a trustee in making an appropriate allocation between income and principal beneficiaries. In other cases, however, it may be very difficult for a trustee to reconstruct the nature of the expense allocated to the legacy during the succession administration, thus making it impossible for the trustee to reliably allocate the expense within the trust between the income and principal beneficiaries. This provision attempts to provide the trustee with flexibility in allocating receipts and expenses and at the same time achieve consistency with the rules on successions and other provisions of the Louisiana Trust Code. See, e.g., Civil Code Article 1426 and R.S. 9:2151, 2152(A)(4), 2153(A), and 2154(A).

(c) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2149. ~~Corporate distributions~~ Receipts from interests in juridical persons

~~A. Corporate distributions of shares of the distributing corporation, including distributions in the form of a stock split or stock dividend, are principal. A right to subscribe to shares or other securities issued by the distributing corporation accruing~~

~~to stockholders on account of their stock ownership and the proceeds of any sale of the right are principal.~~

~~B. Except to the extent that the corporation indicates that some part of a corporate distribution is a settlement of preferred or guaranteed dividends accrued since the trustee became a stockholder or is in lieu of an ordinary cash dividend, a corporate distribution is principal if the distribution is pursuant to:~~

~~(1) A call of shares;~~

~~(2) A merger, consolidation, reorganization, or other plan by which assets of the corporation are acquired by another corporation; or~~

~~(3) A total or partial liquidation of the corporation, including any distribution that the corporation indicates is a distribution in total or partial liquidation, or any distribution of assets, other than cash, pursuant to a court decree or final administrative order by a government agency ordering distribution of the particular assets.~~

~~C. Distributions made from ordinary income by a regulated investment company or by a trust qualifying and electing to be taxed under federal law as a real estate investment trust are income. All other distributions made by the company or trust, including distributions from capital gains, depreciation, or depletion, whether in the form of cash or an option to take new stock or cash or an option to purchase additional shares, are principal.~~

~~D. All other corporate distributions are income, including cash dividends, distributions of, or rights to subscribe to, shares, securities, or obligations of corporations other than the distributing corporation, and the proceeds of the rights or of the property distributions, except as Sub-sections A, B, or C above provide otherwise.~~

~~E. If the distributing corporation gives a stockholder an option to receive a distribution either in cash or in its own shares, the distribution chosen is income, except as provided in Sub-sections B and C of this section.~~

~~F. A trustee may rely upon any statement of the distributing corporation as to any fact relevant under any provision of this Sub-part concerning the source or character of dividends or distributions of corporate assets.~~

A. Except as otherwise provided in this Section, a trustee shall allocate to income money received on account of an interest in a juridical person.

B. A trustee shall allocate to principal the following distributions received on account of a trustee's interest in a juridical person:

(1) Property other than money.

(2) Money received in one distribution or a series of related distributions in exchange for part or all of a trustee's interest in the juridical person.

(3) Money received in total or partial liquidation of the juridical person.

(4) Money received from a regulated investment company or a real estate investment trust if the money distributed is a capital gain dividend for federal income tax purposes.

C. Money is received in partial liquidation to the extent that the juridical person, at or near the time of a distribution, indicates that it is a distribution in partial liquidation. A partial liquidation also occurs if the total amount of money and property received in a distribution or series of related distributions is greater than twenty percent of the juridical person's gross assets, as shown by the juridical person's year-end financial statements immediately preceding the initial receipt.

D. Money is not received in partial liquidation, nor may it be taken into account under Subsection C of this Section, to the extent that it does not exceed the amount of income tax that a trustee or beneficiary must pay on taxable income of the juridical person that distributes the money.

E. Notwithstanding the provisions of this Section, if the receipt is one to which a more specific provision of this Subpart applies, a trustee may allocate the receipt based upon the source or character of the receipt and may rely upon a statement made by the juridical person regarding the source or character of the receipt.

Revision Comments - 2020

(a) This revision is based upon Section 401 of the 1997 version of the Uniform Principal and Income Act. Prior law contained in R.S. 9:2149 and 2150 was adopted verbatim (with the exception of R.S. 9:2149(D)) from the 1962 version of the UPIA. At the time of that Act, the dominant business form was the corporation. Thus, both the UPIA of 1962 and prior Louisiana law made no mention of limited liability companies or other modern business forms. The new UPIA of 1997 retains the same basic principles as the 1962 version but broadens the types of business forms to which the law is applicable. Given the multitude of types of juridical persons, it is not feasible to continue the old schematic that listed the various types of property that would be classified as principal. The 1997 UPIA and this revision classify all non-monetary property as principal and thus include all of the prior categories of property that were classified as principal.

(b) A cash distribution may be large (for example, more than 10% but not more than 20% of a juridical person's assets) and have characteristics that suggest it should be treated as principal rather than income. For example, a juridical person may have received cash from a source other than the conduct of its normal business operations because it sold an investment asset; or it sold a business asset other than one held for sale to customers in the normal course of business and did not replace it; or it borrowed a large sum of money and secured the repayment of the loan with a substantial asset; or a principal source of its cash was from assets such as mineral interests, 90% of which would have been allocated to principal if the trust had owned the assets directly. In such a case the trustee, after considering the total return from the portfolio as a whole and the income component of that return, may decide to exercise the power under R.S. 9:2158 to make an adjustment between income and principal.

(c) Subsection E of this Section provides the trustee with discretion to make an allocation regarding a receipt in accordance with the other provisions of this Section or in accordance with the source of the receipt, provided a more specific rule governs the source of the receipt in this Part. For instance, if the source of the receipt is due to the trustee's interest in a limited liability company deriving funds from minerals, then the trustee may allocate the receipt in accordance with the provisions of this Section or in accordance with the provisions of R.S. 9:2152. In making the allocation, Subsection E also provides the trustee with the authority to rely upon a statement of the relevant juridical person as to the source of the receipt without requiring the trustee to otherwise ascertain its source.

(d) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2150. ~~Bonds~~ <u>Obligation to pay money</u>

~~A. Bonds or other obligations for the payment of money are principal at their inventory value, except as provided in Sub-section B below. No provision shall be made for amortization of bond premiums or for accumulation for discount. The proceeds of sale, redemption, or other disposition of the bonds or obligations are principal.~~

~~B. The increment in value of a bond or other obligation for the payment of money payable at a future time in accordance with a fixed schedule of appreciation in excess of the price at which it was issued is income. The increment in value is distributable at the time provided in R.S. 9:1841 through 9:1847, R.S. 9:1891 through 9:1906, and R.S. 9:1961 through 9:1965, from the first principal cash available to the beneficiary who was the income beneficiary at the time of increment. If unrealized increment is distributed as income but out of principal, the principal shall be reimbursed for the increment when realized.~~

<u>A. An amount received as interest, whether determined at a fixed, variable, or floating rate, on an obligation to pay money to the trustee, including an amount received in return for prepaying principal, shall be allocated to income without any provision for amortization of premium.</u>

<u>B. A trustee shall allocate to principal an amount received from the sale, redemption, or other disposition of an obligation to pay money to the trustee more than one year after it is purchased or acquired by the trustee, including an obligation whose purchase price or value when it is acquired is less than its value at maturity. If the obligation matures within one year after it is purchased or acquired by the trustee, an amount received in excess of its purchase price or its value when acquired by the trust shall be allocated to income.</u>

<u>C. This Section does not apply to an obligation to which R.S. 9:2151.2, 2152, 2153, or 2154 applies.</u>

Revision Comments - 2020

(a) This revision is based upon Section 406 of the UPIA (1997).

(b) This revision changes the law by providing that the entire increase in value of discount obligations is attributable to principal when the trustee receives the proceeds from the disposition, unless the obligation, when acquired, has a maturity of less than one year.

(c) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2151. ~~Business operations~~ Sole proprietorship

~~If a trustee uses any part of the principal in the operation of a business of which, as trustee, he is a proprietor or a partner, the proceeds and losses of the business~~ The receipts and expenses of a sole proprietorship shall be allocated in accordance with what is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal~~, and in view of the manner in which men of ordinary prudence, discretion, and intelligence would act in the management of their own affairs~~.

Revision Comments - 2020

(a) This revision modifies existing law to make clear that this provision applies only to a trustee's operation of a sole proprietorship. The operation of other business forms is treated in R.S. 9:2149.

(b) A sole proprietorship is not a separate juridical person in Louisiana, but merely a method of doing business in which an individual personally owns the assets and retains the liabilities of a business. See, e.g., *Robinson v. Heard*, 809 So. 2d 943, 946 (La. 2002) ("A sole proprietorship is not a legal entity. It is merely a designation assigned to a manner of doing business by an individual. While the individual involved in the sole proprietorship may consider the business to be separate and distinct from his/her person, there exists no legal distinction between the individual and the business.").

(c) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2151.1. Insurance contracts

A. A trustee shall allocate to principal the proceeds of a life insurance policy in which the trustee is named as beneficiary.

B. A trustee shall allocate to principal the proceeds of a contract that insures the trustee against loss for damage to, destruction of, or loss of an interest in a trust asset.

C. The trustee shall allocate dividends on an insurance policy to income if the premiums on the policy are paid from income, and to principal if the premiums are paid from principal.

D. A trustee shall allocate to income proceeds of a contract that insures the trustee against loss of occupancy or other use by an income beneficiary, loss of income, or loss of profits from a business.

Revision Comments - 2020

This revision is based upon Section 407 of the UPIA (1997). The term "proceeds," as used in this Section, refers to the insurable benefit under the contract and does not include other payments associated with the benefit, such as interest.

§2151.2. Deferred compensation, annuities, and similar payments

A. Payments made in money or other property to a trustee over a period of years or during the life of an individual from an annuity, an individual retirement account, an employee-benefit plan, a pension plan, a profit-sharing plan, a deferred compensation plan, or any similar arrangement created pursuant to income-tax incentives to fund for retirement are allocated as follows:

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

(2) If no part of a payment is characterized as interest, a dividend, or an equivalent, and all or part of the payment is required to be made, a trustee shall allocate to income ten percent of the part that is required to be made during the accounting period and the balance to principal. If no part of a payment is required to be made or the payment received is the entire amount to which the trustee is entitled, the trustee shall allocate the entire payment to principal. To the extent that a trustee exercises a right of withdrawal, a payment is not considered to be required to be made.

B. If, in order to qualify for a marital deduction, a trustee must allocate more of a payment to income than provided for in this Section, the trustee shall allocate to income the additional amount necessary to qualify for the marital deduction.

Revision Comments - 2020

(a) This provision is based, in part, on Section 409 of the UPIA (1997) and informed by statutes from other states that have modified Section 409 of the UPIA. See, e.g., Mass. Gen. Law. Ann. 203D-18; N. J. Stat. Ann. 3B:19B-17; N.Y. Estate, Prob. & Tr. Law 11-A-4.9; Alaska Rev. Stat. 13.38.690; Hawaii Rev. Stat. 557A-409; Ohio. Rev. Code 5812.32.

(b) This Section applies to amounts received by a trustee under contractual arrangements that provide for payments to a third-party beneficiary as a result of services rendered or property transferred to a payer in exchange for future payments. It applies whether the payments begin when the payment right becomes subject to the trust or are deferred until a future date, and it applies whether payments are made in cash or in kind, such as employer stock. In-kind payments usually will be made in a single distribution that will be allocated to principal under the second sentence of Paragraph (A)(2).

(c) Paragraph (A)(1) applies only to certain types of deferred compensation, phantom stock plans, and similar plans whose terms characterize a payment as dividends or interest. It does not apply to individual retirement accounts and similar arrangements. Paragraph (A)(2) applies to required payments from an IRA or similar arrangement.

(d) Paragraph (A)(2) of this Section differentiates between payments that are required to be made and all other payments. To the extent that a payment is required to be made (either under federal income tax rules, or, in the case of a plan that is not subject to those rules, under the terms of the plan), 10% of the amount received is allocated to income and the balance to principal. The right to receive payments under this Paragraph is a type of liquidating asset and therefore is treated similarly to property subject to depletion under R.S. 9:2154. All other payments are allocated to principal because they represent a change in the form of the principal asset. To that extent, this rule follows the general policy of R.S. 9:2144, which provides that property received in replacement of property shall be allocated to principal.

(e) Under Revenue Ruling 2006-26, the Internal Revenue Service declared that the 10% allocation provided in Section 409 of the UPIA did not qualify for the IRS's safe harbors, as 10% of a required minimum distribution is not a reasonable apportionment of the total return of the trust between income and principal. Under the ruling, the trustee is required to make available to the beneficiary the income of an IRA or defined contribution plan in order to qualify. To comply with the ruling, Section 409 of the UPIA was amended in 2008 to provide separate rules for determining the income of a marital trust that is the beneficiary of an IRA or similar arrangement. This revision simplifies the provisions of the UPIA while, at the same time, allowing the preservation of the marital deduction.

§2152. Proceeds of mineral interests

~~A. If any part of the principal consists of a right to receive royalties or overriding royalties, production from working interests or production payments, proceeds from net profits interests or payments for the right to extract minerals from immovable property, or other interests in oil, gas, and other minerals, the allocation of the proceeds of such interests shall be made as follows:~~

~~(1) If received as a delay rental on a lease, extension of payments on a lease, shut-in royalty, or bonus for the execution of a lease, the proceeds shall be allocated to income;~~

~~(2) If received from a production payment, then to the extent of any stated factor for interest or its equivalent, the proceeds shall be allocated to income; the~~

~~balance of such proceeds shall be apportioned between principal and income by allocating to principal the fraction thereof that the unrecovered cost of the production payment bears to the remaining balance due upon the production payment (excluding any factor for interest or its equivalent) and by allocating the remainder of such proceeds to income;~~

~~(3) If received from a royalty, overriding royalty, limited royalty, or working interest, net profits interest, or from any other interest in oil, gas, or other minerals, not specifically covered in this section, such proceeds shall be allocated to principal until such time as the cost for such interest (including both tangible and intangible drilling cost) has been fully recovered; thereafter, such proceeds shall be apportioned between principal and income so that twenty-seven and one-half percent of the gross proceeds (but not to exceed fifty percent of the net proceeds remaining after payment of all expenses, direct and indirect, computed without allowances for depletion) shall be allocated to a reserve for depletion to be added to principal and the balance of the gross proceeds, after payment therefrom of all expenses, direct and indirect, shall be allocated to income.~~

~~B. This section is not applicable to timber, water, soil, sod, dirt, turf, mosses, shells, gravel, or other natural resources.~~

A. To the extent that a trustee accounts for receipts from an interest in mineral rights or other interest in oil, gas, or other minerals pursuant to this Section, the trustee shall allocate them as follows:

(1) If received as delay rental or annual rent on a mineral lease, a receipt shall be allocated to income.

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

(3) If received as a royalty, overriding royalty, shut-in-well payment, take-or-pay payment, or bonus, a receipt shall be allocated in accordance with what

is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal.

(4) If an amount is received from a working interest or any other interest not provided for in this Subsection, a receipt shall be allocated in accordance with what is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal.

B. This Section applies whether or not a decedent or donor was extracting oil, gas, or other minerals before the interest became subject to the trust.

C. If the trust property includes an interest in mineral rights or other interest in oil, gas, or other minerals on the effective date of this Act, the trustee may allocate receipts from the interest as provided in this Section or in the manner used by the trustee before the effective date of this Act. If the trustee acquires an interest in mineral rights or other interest in oil, gas, or other minerals after the effective date of this Act, the trustee shall allocate receipts from the interest as provided in this Section.

D. An allocation of a receipt under this Section is presumed to be reasonable and equitable if ninety percent is allocated to principal and ten percent to income. Any other allocation shall not be presumed to be unreasonable or inequitable.

E. This Section is not applicable to timber, water, soil, sod, dirt, turf, mosses, shells, gravel, or other natural resources.

Revision Comments - 2020

(a) This provision is new. It is based upon Texas Property Code Section 116.174 and Section 411 of the UPIA (1997). Unlike the UPIA but like Texas law, this Section allows for allocation of royalty payments associated with oil and gas leases in a manner that is reasonable and equitable. Under Subsection D but unlike the Texas statute, this provision adopts a safe harbor providing that an allocation of ninety percent to principal and ten percent to income is presumed to be reasonable and equitable but at the same time being clear that other allocations are not necessarily unreasonable or inequitable. Prior law allocated the royalty payments associated with oil and gas leases in the amount of 27.5% to principal and 72.5% to income. These percentages have been part of the Trust Code since 1964 and were included at that time because the Internal Revenue Code provided for a 27.5% depletion allowance. At that time, the UPIA of 1962 also provided similarly. The IRC now no longer provides for the 27.5% depletion allowance. As a result, many states have adopted a 90% depletion rate from the 1997 version of the UPIA. See, e.g., Cal. Prob. Code § 16363; Mich. Comp. Laws § 555.811; Colo. Laws. 15-1-421. The rationale for this drastic change is that the old law inappropriately caused a large portion of oil and gas proceeds - 72.5% - to be paid out as income. Over the life of a well, the output would be depleted significantly. Allocating more to principal allows the trustee to obtain other income-producing assets that might still be productive when the minerals are exhausted. The approach adopted by this Section allows the trustee flexibility in the allocation.

(b) Subsection B abolishes the open mines doctrine in trust.

(c) Under Subsection C, the new depletion allowances are made prospectively applicable. For oil and gas interests included in a trust on the effective date of this provision, the trustee has discretion in deciding which method of depletion (i.e., the old or new law) to apply.

(d) Unlike the UPIA and the Texas statute, this provision does not apply to water, timber, gravel, or other natural resources. R.S. 9:2153 and 2154 provide the appropriate rules with respect to timber and other property subject to depletion.

(e) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2153. Timber

A. If part of the principal consists of land from which timber may be removed, the receipts from taking the timber from the land shall be allocated in accordance with what is reasonable and equitable in view of the interests of those entitled to income as well as of those entitled to principal~~, and in view of the manner in which men of ordinary prudence, discretion, and intelligence would act in the management of their own affairs~~.

B. An allocation of a receipt under this Section is presumed to be reasonable and equitable if ninety percent is allocated to principal and ten percent to income. Any other allocation shall not be presumed to be unreasonable or inequitable.

Revision Comments - 2020

(a) This revision updates the language but maintains the "reasonable and equitable" standard. Like R.S. 9:2152, Subsection B adopts a safe harbor providing that an allocation of ninety percent to principal and ten percent to income is presumed to be reasonable and equitable but at the same time being clear that other allocations are not necessarily unreasonable or inequitable. It also deletes the "prudent man" rule that existing under prior law because persons of "ordinary prudence, discretion, and intelligence" do not generally consider the interests of successor beneficiaries in managing their own affairs. See, e.g., UPIA (1997) §103, Comment.

(b) This Section is consistent with the principles of Louisiana property law that generally treat trees as capital assets rather than fruits. In some instances, however, trees in a tree farm or in a regularly exploited forest must be treated as fruits. See, e.g., Civil Code Article 551, Comment (b).

(c) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2154. Other property subject to depletion

A. Except as provided in R.S. 9:2152 and ~~9:2153~~ 2153, if the principal consists of property subject to depletion, ~~receipts from the property not in excess of five percent of its inventory value are income, and the balance is principal~~ the receipts shall be allocated in accordance with what is reasonable and equitable in view of the interests of those entitled to income as well as those entitled to principal.

B. An allocation of a receipt under this Section is presumed to be reasonable and equitable if ninety percent is allocated to principal and ten percent to income. Any other allocation shall not be presumed to be unreasonable or inequitable.

Revision Comments - 2020

(a) This revision updates the law to make the depletion allowance consistent with the "reasonable and equitable" standard in R.S. 9:2153. Like R.S. 9:2152 and 2153, Subsection B adopts a safe harbor providing that an allocation of ninety percent to principal and ten percent to income is presumed to be reasonable and equitable but at the same time being clear that other allocations are not necessarily unreasonable or inequitable.

(b) The Comments that accompanied the 1964 enactment of this provision, which are superseded by the 2020 Revision Comments, appear in Acts 1964, No. 338.

§2156. Charges

A. The following charges shall be made against income:

(1) Ordinary expenses incurred or accrued in connection with the administration, management, or preservation of the trust property~~;~~.

(2) ~~A reasonable allowance for depreciation on property subject to depreciation under generally accepted accounting principles, but no allowance shall be made for depreciation of that portion of immovable property used by a beneficiary as a residence;~~

~~(3)~~ One-half of court costs, ~~attorney's~~ attorney fees, and other fees on periodic accounting, unless the court directs otherwise~~;~~.

~~(4)~~(3) Court costs, ~~attorney's~~ attorney fees, and other fees on other accountings or judicial proceedings if the matter primarily concerns the income interest, unless the court directs otherwise~~;~~.

~~(5)~~(4) One-half of the trustee's regular compensation, whether based on a percentage of principal or income~~;~~.

~~(6)~~(5) Expenses reasonably incurred by the trustee for the management and application of income~~;~~.

~~(7) A tax levied upon receipts defined as income under this Sub-part or the trust instrument and payable by the trustee;~~

~~(8)~~(6) Interest accrued on an indebtedness.

* * *

C. The following charges shall be made against principal:

(1) Extraordinary expenses incurred or accrued in connection with the administration, management, or preservation of the trust property~~;~~.

(2) Expenses incurred in making a capital improvement to principal, including special taxes and assessments~~;~~.

(3) Expenses incurred in investing and reinvesting principal~~;~~.

(4) One-half of court costs, ~~attorney's~~ attorney fees, and other fees on periodic accounting, unless the court directs otherwise~~;~~.

(5) Court costs, ~~attorney's~~ attorney fees, and other fees on other accountings or judicial proceedings if the matter primarily concerns the principal interest, unless the court directs otherwise~~;~~.

(6) Expenses incurred in maintaining or defending an action to construe the trust or to protect the trust or the trust property~~;~~.

(7) One-half of the trustee's regular compensation, whether based on a percentage of principal or income~~;~~.

(8) All the trustee's special compensation~~;~~.

(9) ~~A tax levied upon profit, gain, or other receipts allocated to principal notwithstanding denomination of the tax as an income tax by the taxing authority;~~

~~(10)~~ The amount of an estate tax apportioned to the trust, including interest and penalties~~;~~.

~~(11)~~(10) The principal of an indebtedness~~;~~.

~~(12) All other expenses not chargeable to income.~~

* * *

E. Regularly recurring charges shall be apportioned to the same extent and in the same manner that receipts are apportioned under R.S. 9:2145 through ~~9:2147~~ 2147.

Revision Comments - 2020

This Section deviates from Sections 501, 502, and 504 of the UPIA (1997). Paragraph (A)(2) of the prior law regarding depreciable property has been deleted in favor of a new provision, R.S. 9:2156.1, which is based upon Section 503 of the UPIA. Paragraphs (A)(7) and (C)(9) of the prior law regarding allocation of taxes have been deleted in favor of a new provision, R.S. 9:2156.2. Paragraph (C)(12) of the prior law, which allocated to principal all expenses not otherwise allocated to income, has also been deleted in light of the revision now contained in R.S. 9:2142(3).

§2156.1. Transfers from income to principal for depreciation

A trustee may transfer to principal a reasonable amount of the net cash receipts from a principal asset that is subject to depreciation, but may not transfer any amount for depreciation during the administration of a succession or for that portion of an immovable used or available for use by a beneficiary as a residence or of corporeal movables held or made available for the personal use or enjoyment of a beneficiary. An amount transferred to principal need not be held as a separate fund.

Revision Comments - 2020

(a) This Section is based upon Section 503 of the UPIA (1997). Under Section 503(a) of the UPIA and this Section, the term "depreciation" means a reduction in value due to wear, tear, decay, corrosion, or gradual obsolescence of a fixed asset having a useful life of more than one year.

(b) Under this revision, a transfer to principal for depreciation is discretionary with the trustee. Prior law provided that a charge shall be made against income for "... a reasonable allowance for depreciation under generally accepted accounting principles…" That provision was resisted by many trustees who did not provide for depreciation for a number of reasons. One reason relied upon was that a charge for depreciation was not needed to protect the beneficiaries if the value of the land was increasing; another was that generally accepted accounting principles might not require depreciation to be taken if the property was not part of a business.

This revision allows the trustee more flexibility and broader discretion in taking depreciation.

§2156.2. Income taxes

A. A tax required to be paid by a trustee based on receipts allocated to income shall be paid from income.

B. A tax required to be paid by a trustee based on receipts allocated to principal shall be paid from principal, even if the tax is denominated an income tax by the taxing authority.

C. A tax required to be paid by a trustee on the trust's share of a juridical person's taxable income shall be paid as follows:

(1) From income to the extent that receipts from the juridical person are allocated only to income.

(2) From principal to the extent that receipts from the juridical person are allocated only to principal.

(3) Proportionately from principal and income to the extent that receipts from the juridical person are allocated to both income and principal.

(4) From principal to the extent that the tax exceeds the total receipts from the juridical person.

D. After applying the provisions of this Section, the trustee shall adjust income or principal receipts to the extent that the trust's taxes are reduced because the trust receives a deduction for payments made to a beneficiary.

Revision Comments - 2020

(a) This Section is based upon Section 505 of the UPIA (1997).

(b) When trust property includes an interest in a pass-through entity, such as a partnership or S corporation, the trust must report its share of the juridical person's taxable income regardless of how much the juridical person distributes to the trust. Whether the juridical person distributes more or less than the trust's tax on its share of the juridical person's taxable income, the trustee must pay the taxes and allocate them between income and principal.

(c) Subsection C requires the trustee to pay the taxes on its share of a juridical person's taxable income from income or principal receipts to the extent that receipts from the juridical person are allocable to each. This assures the trust a source of cash to pay some or all of the taxes on its share of the juridical person's taxable income. Subsection D recognizes that a trust normally receives a deduction for amounts distributed to a beneficiary. Accordingly, Subsection D requires the trustee to increase receipts payable to a beneficiary as determined under Subsection C to the extent the trust's taxes are reduced by distributing those receipts to the beneficiary.

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SUBPART F. POWER TO MAKE PROPERTY PRODUCTIVE OF INCOME

§2164. Underproductive property

If a marital deduction is allowed for all or part of a trust whose assets consist substantially of property that does not provide the spouse with sufficient income from or use of the trust assets, and if the amounts that the trustee transfers from principal to income under R.S. 9:2158 and distributes to the spouse from principal pursuant to the terms of the trust are insufficient to provide the spouse an interest required to obtain the marital deduction, the spouse may require the trustee to make property productive of income, convert property within a reasonable time, or exercise the power conferred by R.S. 9:2158. The trustee may decide which action or combination of actions to take.

Revision Comments - 2020

(a) This revision is based upon Section 413(a) of the UPIA (1997).

(b) R.S. 9:2127 provides that "[a] trustee's investment and management decisions are to be evaluated in the context of the trust property as a whole…" The law in prior R.S. 9:2155 gave the income beneficiary a right to receive a portion of the proceeds from the sale of underproductive property as "delayed income." This provision applied on an asset-by-asset basis and not by taking into consideration the trust portfolio as a whole and thus conflicted with the basic precept in R.S. 9:2127. Moreover, in determining the amount of delayed income, the prior law did not permit the trustee to take into account the extent to which the trustee may have distributed principal to the income beneficiary, under principal invasion provisions in the terms of the trust, to compensate for insufficient income from the unproductive asset. Under R.S. 9:2158, a trustee must consider prior distributions of principal to the income beneficiary in deciding whether and to what extent to exercise the power to adjust.

(c) Although this revision abolishes the right to receive delayed income, it allows an income beneficiary's right to compel the trustee to make property productive of income. The duty to make property productive of income should be determined by taking into consideration the performance of the portfolio as a whole and the extent to which a trustee makes principal distributions to the income beneficiary under the terms of the trust and adjustments between principal and income under R.S. 9:2158.

(d) Under this revision, once the surviving spouse makes an appropriate demand that the trustee take action, the trustee must decide whether to make property productive of income, convert it, transfer funds from principal to income, or take some combination of those actions.

Section 2. R.S. 9:2155 and 2157 are hereby repealed in their entirety.

Section 3. The existing Comments to R.S. 9:2148 through 2154 are superseded by the Comments appearing beneath those Sections in this Act. The Louisiana State Law Institute is hereby directed to remove the existing Comments and to print only the Comments appearing in this Act.

Section 4. The Louisiana State Law Institute is hereby directed to redesignate Subpart F of Part V of Chapter 1 of Code Title II of Code Book III of Title 9 of the Louisiana Revised Statutes of 1950, entitled "THE TRUSTEE'S BOND," as Subpart G of Part V of Chapter 1 of Code Title II of Code Book III of Title 9 of the Louisiana Revised Statutes of 1950, and to retain the heading of this Subpart.

Section 5. The provisions of this Act shall become effective on January 1, 2021. Except as specifically provided in this Act or in the provisions of the trust, the provisions of this Act apply to trusts existing as of the effective date of this Act.

DIGEST

The digest printed below was prepared by House Legislative Services. It constitutes no part of the legislative instrument. The keyword, one-liner, abstract, and digest do not constitute part of the law or proof or indicia of legislative intent. [R.S. 1:13(B) and 24:177(E)]

HB 123 Original 2020 Regular Session Gregory Miller

Abstract: Provides for the allocation of receipts and expenses to income and principal in trusts.

Present law (R.S. 9:2141) provides the general rule for the allocation of receipts and expenditures in the administration of trusts.

Proposed law retains present law but makes changes in terminology.

Present law (R.S. 9:2142) provides that trust receipts and expenditures shall be allocated to income or principal in accordance with the provisions of the trust instrument or in accordance with the provisions of the Trust Code. In the absence of such provisions, present law provides that trust receipts and expenditures shall be allocated entirely to principal.

Proposed law retains present law but provides that in the absence of allocation provisions in the trust instrument or in the Trust Code, trust receipts and expenses shall be allocated in accordance with what is reasonable and equitable.

Present law (R.S. 9:2143) provides for the allocation of receipts and expenditures to the beneficiaries of usufruct and naked ownership. In the absence of provisions concerning allocation in the trust instrument or in the Trust Code, present law employs the "prudent man" standard in providing that trust receipts and expenses shall be allocated in accordance with what is reasonable and equitable.

Proposed law retains present law but makes semantic changes and removes the "prudent man" standard as inapplicable.

Present law (R.S. 9:2144) provides for the distinction between income and principal.

Proposed law retains present law but makes semantic changes.

Present law (R.S. 9:2145) provides when the right to income arises.

Proposed law retains present law but makes semantic changes.

Present law (R.S. 9:2146) provides for the apportionment of receipts when the right to income arises, including receipts in the form of periodic payments such as corporate distributions to stockholders.

Proposed law expands the applicability of present law to also include receipts from interests in juridical persons other than corporations, such as limited liability companies and other modern business forms.

Present law (R.S. 9:2147) provides for the apportionment of receipts when the right to income ceases, including income in the form of periodic payments such as corporate distributions to stockholders.

Proposed law expands the applicability of present law to also include receipts from interests in juridical persons other than corporations, such as limited liability companies and other modern business forms.

Present law (R.S. 9:2148) provides that succession receipts and expenses shall be allocated in accordance with the laws regulating donations mortis causa.

Proposed law changes present law by no longer deferring to the Civil Code with respect to the allocation of succession receipts and expenses and instead applying the general rule that the allocation shall be made in accordance with what is reasonable and equitable.

Present law (R.S. 9:2149) provides for the allocation of corporate distributions and categorizes the specific types of property that are classified as principal.

Proposed law expands the applicability of present law to also include receipts from interests in juridical persons other than corporations, such as limited liability companies and other modern business forms. As a result, proposed law more generally classifies all non-monetary property as principal.

Present law (R.S. 9:2150) provides for the allocation of bonds or other obligations to pay money.

Proposed law changes present law to conform with uniform law by providing that the entire increase in value of discount obligations is attributable to principal when the trustee receives the proceeds from the disposition, unless the obligation, when acquired, has a maturity of less than one year.

Present law (R.S. 9:2151) provides for the allocation of proceeds and losses in the operation of a business of which the trustee is a proprietor or partner.

Proposed law changes present law by clarifying that this provision applies only to the trustee's operation of a sole proprietorship, which would not be considered a juridical person under proposed law (R.S. 9:2149). Proposed law also eliminates the "prudent man" standard as inapplicable.

Proposed law (R.S. 9:2151.1) provides for the allocation of proceeds from insurance contracts.

Proposed law (R.S. 9:2151.2) provides for the allocation of payments made from annuities, individual retirement accounts, and deferred compensation, pension, employee-benefit, or other similar plans.

Present law (R.S. 9:2152) provides for the allocation of proceeds of mineral interests and allocates the royalty payments associated with oil and gas leases in the amount of 27.5% to principal and 72.5% to income.

Proposed law changes present law by providing that royalty payments shall be allocated in accordance with what is reasonable and equitable. Proposed law further provides that allocation of 90% to principal and 10% to income is presumed to be reasonable and equitable but clarifies that other allocations are not necessarily unreasonable or inequitable. Proposed law also abolishes the open mines doctrine in trust.

Proposed law provides that the new depletion allowances are made prospectively applicable but clarifies that for oil and gas interests included in an existing trust, the trustee has discretion in deciding whether to apply the method of depletion under present law or proposed law.

Present law (R.S. 9:2153) provides that receipts from timber shall be allocated in accordance with what is reasonable and equitable.

Proposed law retains present law but eliminates the "prudent man" standard as inapplicable. Proposed law further provides that allocation of 90% to principal and 10% to income is presumed to be reasonable and equitable but clarifies that other allocations are not necessarily unreasonable or inequitable.

Present law (R.S. 9:2154) provides that receipts from other property subject to depletion not in excess of five percent of its inventory value are income, and the balance is principal.

Proposed law changes present law to provide that receipts from other property subject to depletion shall be allocated in accordance with what is reasonable and equitable. Proposed law further provides that allocation of 90% to principal and 10% to income is presumed to be reasonable and equitable but clarifies that other allocations are not necessarily unreasonable or inequitable.

Present law (R.S. 9:2156) provides for charges to be made against income and principal, including charges concerning depreciable property and taxes. Present law also provides that all other expenses not chargeable to income shall be charged to principal.

Proposed law retains present law but makes semantic changes and eliminates charges concerning depreciable property and taxes now included in proposed law (R.S. 9:2156.1 and 2156.2). Proposed law also eliminates the rule in present law that all other expenses not chargeable to income shall be charged to principal, since the default rule is now that receipts and expenses shall be allocated in accordance with what is reasonable and equitable, rather than entirely to principal.

Proposed law (R.S. 9:2156.1) changes present law by providing the trustee with discretion to make transfers from income to principal for property that is subject to depreciation, rather than allowing such charges against income to occur in accordance with generally accepted accounting principles.

Proposed law (R.S. 9:2156.2) provides for the payment of taxes from income based on receipts allocated to income and for the payment of taxes from principal based on receipts allocated to principal. Proposed law further provides for the payment of taxes on the trust's share of a juridical person's taxable income from income, principal, or both proportionately and requires the trustee to adjust income or principal receipts in the event that the trust receives a deduction for payments made to a beneficiary.

Present law (R.S. 9:2157) defines the term "inventory value".

Proposed law repeals the present law definition of "inventory value", a term that is no longer used.

Present law (R.S. 9:2155) provides the income beneficiary with a right to receive a portion of the proceeds from the sale of underproductive property as "delayed income" and applies on an asset-by-asset basis.

Proposed law repeals present law.

Proposed law (R.S. 9:2164) provides the income beneficiary with the right to compel the trustee to take action to make property productive of income, convert the property within a reasonable time, transfer funds from principal to income, or take some combination of those actions.

(Amends R.S. 9:2141 - 2144, 2145(1), 2146, 2147-2154, and 2156(A), (C), and (E); Adds R.S. 9:2151.1, 2151.2, 2156.1, 2156.2, and 2164; Repeals R.S. 9:2155 and 2157)