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1 (A) a court-appointed guardian of an incapacitated beneficiary;

2 (B) an agent for an incompetent beneficiary; and

3 (C) a court-appointed guardian of a minor beneficiary's estate;

4 (13) "trust" includes a revocable trust, an irrevocable trust, and a legal  
5 life estate arrangement;

6 (14) "trustee" includes an original, additional, or successor trustee,  
7 whether or not appointed or confirmed by a court;

8 (15) "unitrust" means a trust from which a fixed percentage of the net  
9 fair market value of the trust's assets, valued annually, is paid not less often than  
10 annually to a beneficiary.

11 **Sec. 13.38.990. Short title.** This chapter may be cited as the Alaska Principal  
12 and Income Act.

13 \* **Sec. 3.** AS 37.14.031(d) is amended to read:

14 (d) The authority shall adopt regulations providing for the determination  
15 of [PROVISIONS OF AS 13.38 APPLY TO DETERMINE] amounts attributable to  
16 [THE] principal under (b)(2) of this section. The regulations must provide for the  
17 allocation between principal and income of money received from the  
18 management of mental health trust land, and the manner of allocation must be in  
19 the long-term best interest of the trust and its beneficiaries.

20 \* **Sec. 4.** AS 13.16.550; AS 13.38.010, 13.38.020, 13.38.030, 13.38.040, 13.38.050,  
21 13.38.060, 13.38.070, 13.38.080, 13.38.090, 13.38.100, 13.38.110, 13.38.120, 13.38.130, and  
22 13.38.140 are repealed.

23 \* **Sec. 5.** The uncodified law of the State of Alaska is amended by adding a new section to  
24 read:

25 **APPLICABILITY.** AS 13.38.200 - 13.38.990, enacted by sec. 2 of this Act, apply,  
26 except as otherwise expressly provided in the governing instrument, and except as provided  
27 by AS 13.38.900, enacted by sec. 2 of this Act, to a trust existing on or after the effective date  
28 of this Act, and to the estate of a decedent who dies on or after the effective date of this Act.

29 \* **Sec. 6.** This Act takes effect September 1, 2003.

23-LS0366U  
Bannister  
5/2/03

HOUSE CS FOR SENATE BILL NO. 87( )  
IN THE LEGISLATURE OF THE STATE OF ALASKA  
TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:  
Referred:

Sponsor(s): SENATOR SEEKINS

A BILL  
FOR AN ACT ENTITLED

1 "An Act relating to principal and income in the administration of trusts and decedents'  
2 estates and the mental health trust fund; adopting a version of the Uniform Principal  
3 and Income Act; and providing for an effective date."

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

5 \* Section 1. AS 13.36.335 is amended to read:

6 Sec. 13.36.335. Application of special distribution provisions. The asset  
7 distribution provisions of AS 13.16.540 - 13.16.545 [AS 13.16.540 - 13.16.550],  
8 13.16.560, and the provisions of AS 13.38 [AS 13.38.030(a)] apply to the  
9 administration of a revocable trust following the death of the settlor of the trust, unless  
10 the terms of the trust indicate a different intention.

11 \* Sec. 2. AS 13.38 is amended by adding new sections to read:

12 Article 1. Preliminary Provisions; Power to Adjust.

13 Sec. 13.38.200. Fiduciary duties; general principles. (a) In allocating  
14 receipts and disbursements to or between principal and income and with respect to any

1 matter within the scope of this chapter, a fiduciary

2 (1) shall administer a trust or estate in accordance with the governing  
3 instrument, even if there is a different provision in this chapter;

4 (2) may administer a trust or estate by the exercise of a discretionary  
5 power of administration regarding a matter within the scope of this chapter given to  
6 the fiduciary by the governing instrument, even if the exercise of the power produces a  
7 result different from a result required or permitted by this chapter; an inference that  
8 the fiduciary has improperly exercised the discretionary power does not arise from the  
9 fact that the fiduciary has made an allocation contrary to a provision of this chapter;

10 (3) shall administer a trust or estate in accordance with this chapter if  
11 the governing instrument does not contain a different provision or does not give the  
12 fiduciary a discretionary power of administration regarding a matter within the scope  
13 of this chapter; and

14 (4) shall add a receipt or charge a disbursement to principal to the  
15 extent that the governing instrument and this chapter do not provide a rule for  
16 allocating the receipt or disbursement to or between principal and income.

17 (b) In exercising a discretionary power of administration regarding a matter  
18 within the scope of this chapter, whether granted by the governing instrument or this  
19 chapter, including AS 13.38.210 and 13.38.300 - 13.38.410, a fiduciary shall  
20 administer a trust or estate impartially based on what is fair and reasonable to all of the  
21 beneficiaries, except to the extent that the governing instrument clearly manifests an  
22 intention that the fiduciary shall or may favor one or more of the beneficiaries. A  
23 determination in accordance with this chapter is presumed to be fair and reasonable to  
24 all of the beneficiaries.

25 **Sec. 13.38.210. Trustee's power to adjust.** (a) Subject to (c) and (f) of this  
26 section, a trustee may adjust between principal and income by allocating an amount of  
27 income to principal or an amount of principal to income to the extent the trustee  
28 considers appropriate if

29 (1) the governing instrument describes what may or shall be distributed  
30 to a beneficiary by referring to the trust's income;

31 (2) the trustee determines, after applying the rules in AS 13.38.200(a),

1 that the trustee is unable to comply with AS 13.38.200(b); and

2 (3) the trustee determines to follow an investment policy seeking a  
3 total return for the investments held by the trust, whether the return is to be derived  
4 from

5 (A) appreciation of capital;

6 (B) earnings and distributions from capital; or

7 (C) both (A) and (B) of this paragraph.

8 (b) In deciding whether and to what extent to exercise the power conferred by  
9 (a) of this section, a trustee may consider, among other things,

10 (1) the size of the trust;

11 (2) the nature and estimated duration of the trust;

12 (3) the liquidity and distribution requirements of the trust;

13 (4) the need for regular distributions and preservation and appreciation  
14 of capital;

15 (5) the expected tax consequences of an adjustment;

16 (6) the net amount allocated to income under the other sections of this  
17 chapter and the increase or decrease in the value of the principal assets, which the  
18 trustee may estimate as to assets for which market values are not readily available;

19 (7) the assets held in the trust; the extent to which the assets consist of  
20 financial assets, interests in closely held enterprises, tangible and intangible personal  
21 property, or real property; the extent to which an asset is used by a beneficiary; and  
22 whether an asset was purchased by the trustee or received from the settlor or testator;

23 (8) to the extent reasonably known to the trustee, the need of the  
24 beneficiaries for present and future distributions authorized or required by the  
25 governing instrument;

26 (9) whether and to what extent the governing instrument gives the  
27 trustee the power to invade principal or accumulate income or prohibits the trustee  
28 from invading principal or accumulating income, and the extent to which the trustee  
29 has exercised a power from time to time to invade principal or accumulate income;

30 (10) the intent of the settlor or testator; and

31 (11) the actual and anticipated effect of economic conditions on

1 principal and income and the effects of inflation and deflation.

2 (c) A trustee may not make an adjustment under this section if

3 (1) the adjustment would diminish the income interest in a trust that  
4 requires all of the income to be paid at least annually to a spouse and for which a  
5 federal estate tax or gift tax marital deduction would be allowed, in whole or in part, if  
6 the trustee did not have the power to make the adjustment; the prohibition in this  
7 paragraph does not apply to a trust after the trustee determines that the marital  
8 deduction has not been claimed or has not been allowed;

9 (2) the adjustment would reduce the actuarial value of the income  
10 interest in a trust to which a person transfers property with the intent to qualify for a  
11 federal gift tax exclusion;

12 (3) the adjustment would change the amount payable to a beneficiary  
13 as a fixed annuity or a fixed fraction of the value of the trust assets;

14 (4) the adjustment is from any amount that is permanently set aside for  
15 charitable purposes under the governing instrument and for which a federal estate or  
16 gift tax charitable deduction has been taken, unless both income and principal are  
17 permanently set aside for charitable purposes under the governing instrument;

18 (5) possessing or exercising the power to make an adjustment would  
19 cause an individual to be treated as the owner of all or part of the trust for federal  
20 income tax purposes, and the individual would not be treated as the owner if the  
21 trustee did not possess the power to make an adjustment;

22 (6) possessing or exercising the power to make an adjustment would  
23 cause all or part of the trust assets to be subject to federal estate or gift tax with respect  
24 to an individual, and the assets would not be subject to federal estate or gift tax with  
25 respect to the individual if the trustee did not possess the power to make an  
26 adjustment;

27 (7) the trustee is a beneficiary of the trust; or

28 (8) the trust has been converted to a unitrust under AS 13.38.300 -  
29 13.38.410.

30 (d) If (c)(5), (6), or (7) of this section applies to a trustee and there is more  
31 than one trustee, a co-trustee to whom the provision does not apply may make the

1 adjustment unless the exercise of the power by the remaining trustee or trustees is  
2 prohibited by the governing instrument.

3 (e) A trustee may release the entire power conferred by (a) of this section, the  
4 power to adjust from income to principal, or the power to adjust from principal to  
5 income if the trustee is uncertain about whether possessing or exercising the power  
6 will cause a result described in (c)(1) - (6) of this section. or if the trustee determines  
7 that possessing or exercising the power will or may deprive the trust of a tax benefit or  
8 impose a tax burden not described in (c) of this section. The release may be  
9 permanent or for a specified period, including a period measured by the life of an  
10 individual.

11 (f) A governing instrument that limits the power of a trustee to make an  
12 adjustment between principal and income does not affect the application of this  
13 section unless it is clear from the governing instrument that it is intended to deny the  
14 trustee the power of adjustment conferred by (a) of this section.

15 **Sec. 13.38.220. Judicial control of discretionary powers.** (a) A court may  
16 not change a fiduciary's decision to exercise or not to exercise a discretionary power  
17 conferred by this chapter unless the court determines that the decision was an abuse of  
18 the fiduciary's discretion.

19 (b) If a court determines that a fiduciary has abused the fiduciary's discretion  
20 regarding a discretionary power conferred by this chapter, the remedy is to restore the  
21 income and remainder beneficiaries to the positions they would have occupied if the  
22 fiduciary had not abused the fiduciary's discretion, according to the following rules:

23 (1) to the extent that the abuse of discretion has not resulted in a  
24 distribution to a beneficiary or has resulted in a distribution that is too small, the court  
25 shall require the fiduciary to distribute from the trust an amount to the beneficiary that  
26 the court determines will restore the beneficiary, in whole or in part, to the  
27 beneficiary's appropriate position;

28 (2) to the extent that the abuse of discretion has resulted in a  
29 distribution to a beneficiary that is too large, the court shall restore the beneficiaries,  
30 the trust, or both, in whole or in part, to their appropriate positions by requiring the  
31 fiduciary to withhold an amount from one or more future distributions to the

1 beneficiary who received the distribution that was too large or by requiring that  
2 beneficiary or that beneficiary's estate to return some or all of the distribution to the  
3 trust, notwithstanding a spendthrift or similar provision;

4 (3) if the abuse of discretion concerns the power to convert a trust into  
5 a unitrust, the court shall require the trustee either to convert into a unitrust or to  
6 reconvert from a unitrust;

7 (4) to the extent that the court is unable, after applying (1) - (3) of this  
8 subsection, to restore the beneficiaries, the trust, or both to the positions they would  
9 have occupied if the fiduciary had not abused the fiduciary's discretion, the court may  
10 require the fiduciary to pay an appropriate amount from the fiduciary's own funds to  
11 one or more of the beneficiaries, the trust, or both.

## 12 Article 2. Conversion to Unitrust.

13 **Sec. 13.38.300. Power to convert to unitrust.** Unless expressly prohibited  
14 by the governing instrument, a trustee may release the power to adjust under  
15 AS 13.38.210 and may convert a trust into a unitrust as described in AS 13.38.300 -  
16 13.38.410 if

17 (1) the trustee determines that the conversion will enable the trustee to  
18 better carry out the intent of the settlor or testator and the purposes of the trust;

19 (2) the trustee gives written notice of the trustee's intention to release  
20 the power to adjust, of the trustee's intention to convert the trust into a unitrust, and of  
21 how the unitrust will operate, including what initial decisions the trustee will make  
22 under this section, to all the sui juris beneficiaries who

23 (A) are currently eligible to receive income from the trust;

24 (B) would be eligible, if a power of appointment were not  
25 exercised, to receive income from the trust if the interest of all of the  
26 beneficiaries eligible to receive income under (A) of this paragraph were to  
27 terminate immediately before the giving of the notice; and

28 (C) would, if a power of appointment were not exercised,  
29 receive a distribution of principal if the trust were to terminate immediately  
30 before the giving of the notice;

31 (3) there are at least one sui juris beneficiary under (2)(A) of this

1 section and at least one sui juris beneficiary under (2)(B) or (C) of this section; and

2 (4) a sui juris beneficiary does not object to the conversion to a unitrust  
3 in a writing delivered to the trustee within 60 days after the mailing of the notice under  
4 (2) of this section.

5 **Sec. 13.38.310. Judicially approved conversion.** (a) A trustee may petition  
6 the court to approve the conversion to a unitrust if

7 (1) a beneficiary timely objects to the conversion to a unitrust; or

8 (2) there is not a sui juris beneficiary who is eligible under  
9 AS 13.38.300(2)(A), and there is not a sui juris beneficiary who is eligible under  
10 AS 13.38.300(2)(B) or (C).

11 (b) A beneficiary may request a trustee to convert to a unitrust. If the trustee  
12 does not convert, the beneficiary may petition the superior court to order the  
13 conversion.

14 (c) The superior court shall approve the conversion or direct the requested  
15 conversion if the court concludes that the conversion will enable the trustee to better  
16 carry out the intent of the settlor or testator and the purposes of the trust.

17 **Sec. 13.38.320. Factors to be considered.** In deciding whether to exercise  
18 the power conferred by AS 13.38.300, a trustee may consider, among other things,

19 (1) the size of the trust;

20 (2) the nature and estimated duration of the trust;

21 (3) the liquidity and distribution requirements of the trust;

22 (4) the need for regular distributions and preservation and appreciation  
23 of capital;

24 (5) the expected tax consequences of the conversion;

25 (6) the assets held in the trust; the extent to which they consist of  
26 financial assets, interests in closely held enterprises, tangible and intangible personal  
27 property, or real property; and the extent to which an asset is used by a beneficiary;

28 (7) to the extent reasonably known to the trustee, the need of the  
29 beneficiaries for present and future distributions authorized or required by the  
30 governing instrument;

31 (8) whether and to what extent the governing instrument gives the

1 trustee the power to invade principal or accumulate income or prohibits the trustee  
2 from invading principal or accumulating income and the extent to which the trustee  
3 has exercised a power from time to time to invade principal or accumulate income;

4 (9) the actual and anticipated effect of economic conditions on  
5 principal and income and the effects of inflation and deflation.

6 **Sec. 13.38.330. Directions after conversion.** (a) After a trust is converted to  
7 a unitrust, the trustee shall

8 (1) follow an investment policy seeking a total return for the  
9 investments held by the trust, whether the return is to be derived from

10 (A) appreciation of capital;

11 (B) earnings and distributions from capital; or

12 (C) both (A) and (B) of this paragraph; and

13 (2) make regular distributions in accordance with the governing  
14 instrument construed in accordance with the provisions of this section.

15 (b) After a trust has been converted to a unitrust, "income" in the governing  
16 instrument means an annual distribution equal to four percent of the net fair market  
17 value, as determined annually, of the trust's assets, whether the assets would be  
18 considered income or principal under other provisions of this chapter.

19 (c) After a trust has been administered as a unitrust for three years, the four  
20 percent amount referred to in (b) of this section shall be averaged over the three  
21 preceding years of the trust.

22 **Sec. 13.38.340. Discretion of trustee regarding conversion.** The trustee  
23 may in the trustee's discretion, from time to time, determine

24 (1) the effective date of a conversion to a unitrust;

25 (2) the provisions for prorating a unitrust distribution for a short year  
26 in which a beneficiary's right to payments commences or ceases;

27 (3) the frequency of unitrust distributions during the year;

28 (4) the effect of other payments from or contributions to the trust on  
29 the trust's valuation;

30 (5) whether to value the trust's assets annually or more frequently;

31 (6) what valuation dates to use;

1 (7) how frequently to value nonliquid assets and whether to estimate  
2 their value;

3 (8) whether to omit trust property occupied or possessed by a  
4 beneficiary from the calculations; and

5 (9) other matters necessary for the proper functioning of the unitrust.

6 **Sec. 13.38.350. Unitrust deductions and distributions.** (a) Expenses that  
7 would be deducted from income if the trust were not a unitrust may not be deducted  
8 from the unitrust distribution.

9 (b) Unless otherwise provided by the governing instrument, a unitrust  
10 distribution shall be considered to have been paid from net income as net income  
11 would be determined if the trust were not a unitrust. To the extent net income is  
12 insufficient, the unitrust distribution shall be considered to have been paid from net  
13 realized short-term capital gains. To the extent income and net realized short-term  
14 capital gains are insufficient, the unitrust distribution shall be considered to have been  
15 paid from net realized long-term capital gains. To the extent income and net realized  
16 short-term and long-term capital gains are insufficient, the unitrust distribution shall  
17 be paid from the principal of the trust.

18 **Sec. 13.38.360. Court orders regarding unitrust.** The trustee or, if the  
19 trustee declines to petition the court, a beneficiary may petition the court to

20 (1) select a payout percentage different than four percent;

21 (2) provide for a distribution of net income, as would be determined if  
22 the trust were not a unitrust, in excess of the unitrust distribution if the distribution is  
23 necessary to preserve a tax benefit;

24 (3) average the valuation of the trust's net assets over a period other  
25 than three years.

26 **Sec. 13.38.370. Effects of conversion.** A conversion to a unitrust does not  
27 affect a provision in the governing instrument directing or authorizing the trustee to  
28 distribute principal or authorizing a beneficiary to withdraw a portion or all of the  
29 principal.

30 **Sec. 13.38.380. Prohibited conversions; exception.** (a) A trustee may not  
31 convert a trust into a unitrust if

1 (1) payment of the unitrust distribution would change the amount  
2 payable to a beneficiary as a fixed annuity or a fixed fraction of the value of the trust  
3 assets;

4 (2) the unitrust distribution would be made from an amount that is  
5 permanently set aside for charitable purposes under the governing instrument and for  
6 which a federal estate or gift tax deduction has been taken;

7 (3) possessing or exercising the power to convert would cause an  
8 individual to be treated as the owner of all or part of the trust for federal income tax  
9 purposes, and the individual would not be treated as the owner if the trustee did not  
10 possess the power to convert;

11 (4) possessing or exercising the power to convert would cause all or  
12 part of the trust assets to be subject to federal estate or gift tax with respect to an  
13 individual, and the assets would not be subject to federal estate or gift tax with respect  
14 to the individual if the trustee did not possess the power to convert;

15 (5) the conversion would result in the disallowance of a federal estate  
16 tax or gift tax marital deduction that would be allowed if the trustee did not have the  
17 power to convert; or

18 (6) the trustee is a beneficiary of the trust.

19 (b) Notwithstanding (a)(2) of this section, a trustee may elect to convert a trust  
20 to a unitrust if both the income and principal of the trust being converted to a unitrust  
21 are permanently set aside for charitable purposes and if the provisions of  
22 AS 13.38.440 - 13.38.490 are followed.

23 **Sec. 13.38.390. Permissible conversion where otherwise prohibited.** (a) If  
24 AS 13.38.380(a)(3), (4), or (6) applies to a trustee and there is more than one trustee, a  
25 co-trustee to whom the provision does not apply may convert the trust, unless the  
26 exercise of the power by the remaining trustee is prohibited by the governing  
27 instrument.

28 (b) If AS 13.38.380(a)(3), (4), or (6) applies to all the trustees, the trustees  
29 may petition the court to direct a conversion.

30 **Sec. 13.38.400. Reconversion from a unitrust.** A trustee may reconvert a  
31 trust that has been converted into a unitrust under AS 13.38.300 by following the same

1 procedures provided in AS 13.38.300 - 13.38.410 for converting a trust into a unitrust.  
2 If a unitrust is reconverted under this section, the trustee's power to adjust under  
3 AS 13.38.210 applies to the trustee after the reconversion.

4 **Sec. 13.38.410. Release of power to convert to unitrust.** (a) A trustee may  
5 release the power conferred by AS 13.38.300 to convert to a unitrust if the trustee

6 (1) is uncertain about whether possessing or exercising the power will  
7 cause a result described in AS 13.38.380(a)(3), (4), or (5); or

8 (2) determines that possessing or exercising the power will or may  
9 deprive the trust of a tax benefit or impose a tax burden not described in  
10 AS 13.38.380.

11 (b) The release of a power under (a) of this section may be permanent or for a  
12 specified period, including a period measured by the life of an individual.

### 13 **Article 3. Charitable Trust Election.**

14 **Sec. 13.38.440. Charitable trust election.** The trustee of a trust held  
15 exclusively for charitable purposes may elect to be governed by AS 13.38.440 -  
16 13.38.490 unless the governing instrument expressly provides that the election  
17 provided by AS 13.38.440 - 13.38.490 is not available.

18 **Sec. 13.38.450. Eligibility for charitable trust election.** To make an election  
19 under AS 13.38.440 - 13.38.490, the trustee shall adopt and follow an investment  
20 policy seeking a total return for the investments held by the trust, whether the return is  
21 to be derived from appreciation of capital or earnings and distributions with respect to  
22 capital or both. The policy constituting the election must be in writing, must be  
23 maintained as part of the permanent records of the trust, and must recite that it  
24 constitutes an election to be governed by AS 13.38.440 - 13.38.490.

25 **Sec. 13.38.460. Selection of percentage after charitable trust election.** (a)  
26 After a trustee has elected under AS 13.38.440 for the trust to be governed by  
27 AS 13.38.440 - 13.38.490, the trustee shall, in a writing maintained as part of the  
28 permanent records of the trust, select the percentage of the value of the trust that will  
29 be considered income and determine that it is consistent with the long-term  
30 preservation of the real value of the principal of the trust, but the percentage may not  
31 be less than two percent or more than seven percent each year of the principal value of

1 the trust. The trustee may elect to change a percentage previously selected if the  
2 trustee determines that the new percentage is consistent with the long-term  
3 preservation of the real value of the principal of the trust, but may not change the  
4 percentage more frequently than once every 10 years.

5 (b) For a charitable trust required by 26 U.S.C. 4942 (Internal Revenue Code)  
6 to distribute a higher amount than the percentage selected under (a) of this section, the  
7 amount required by 26 U.S.C. 4942 (Internal Revenue Code) controls over the  
8 percentage selected.

9 **Sec. 13.38.470. Revocation of charitable trust election.** The trustee may  
10 revoke an election to be governed by AS 13.38.440 - 13.38.490 if the revocation is  
11 made as part of an alternative investment policy seeking the long-term preservation of  
12 the real value of the principal of the trust. The revocation and alternative investment  
13 policy must be in writing and maintained as part of the permanent records of the trust.

14 **Sec. 13.38.480. Value determination.** For the purposes of applying  
15 AS 13.38.440 - 13.38.490, the value of the trust is the fair market value of the cash  
16 and other assets held by the trustee with respect to the trust, whether these assets  
17 would be considered income or principal under the other provisions of this chapter,  
18 determined at least annually. In the discretion of the trustee, the value of the trust may  
19 be averaged over a period of three or more preceding years when the trust has been  
20 administered as a unitrust under this section for at least three years.

21 **Sec. 13.38.490. Definitions.** In AS 13.38.440 - 13.38.490, except as  
22 otherwise expressly stated in AS 13.38.440 - 13.38.490,

23 (1) "income" means the percentage of the value of the trust computed  
24 under AS 13.38.440 - 13.38.490;

25 (2) "principal" means all assets other than those identified as income in  
26 (1) of this section that are held by the trustee with respect to the trust.

27 **Article 4. Decedent's Estate or Terminating Income Interest.**

28 **Sec. 13.38.500. Determination and distribution of net income.** After a  
29 decedent dies in the case of an estate, or after an income interest in a trust ends, a  
30 fiduciary

31 (1) of an estate or of a terminating income interest shall determine the

1 amount of net income and net principal receipts received from property specifically  
2 given to a beneficiary under (5) of this section and the provisions applicable to trustees  
3 in AS 13.38.550 - 13.38.860; the fiduciary shall distribute the net income and net  
4 principal receipts to the beneficiary who is to receive the specific property;

5 (2) shall distribute to a beneficiary or trust that receives a pecuniary  
6 amount a share of net income equal to the beneficiary's or trust's fractional interest in  
7 undistributed principal assets as determined under AS 13.38.510; the share accrues  
8 from the date of death of a decedent, in the case of an estate, or the date of death of a  
9 settlor or specified event, in the case of a revocable or irrevocable trust;

10 (3) shall determine the remaining net income of a decedent's estate or a  
11 terminating income interest under the provisions applicable to trustees in  
12 AS 13.38.550 - 13.38.860 and by

13 (A) including in net income all income from property used to  
14 discharge liabilities; and

15 (B) paying from principal the debts, the funeral expenses, the  
16 costs of disposition of remains, the family allowance under AS 13.12.404, fees  
17 of personal representatives and their attorneys and accountants, and the taxes,  
18 related interest, and penalties described in AS 13.38.810(a)(7) that are  
19 apportioned to the estate or terminating income interest by the governing  
20 instrument or applicable law;

21 (4) shall distribute the net income remaining after distributions  
22 required by (2) of this section in the manner described in AS 13.38.510 to all other  
23 beneficiaries;

24 (5) may not reduce principal or income receipts from property  
25 described in (1) of this section because of a payment described in AS 13.38.710 or  
26 13.38.720 to the extent that the governing instrument or applicable law requires the  
27 fiduciary to make the payment from assets other than the property or to the extent that  
28 the fiduciary recovers or expects to recover the payment from a third party; the net  
29 income and principal receipts from the property are determined by

30 (A) including all of the amounts the fiduciary receives or pays  
31 with respect to the property, whether those amounts accrued or became due

1 before, on, or after the date of a decedent's death or an income interest's  
2 terminating event; and

3 (B) making a reasonable provision for amounts that the  
4 fiduciary believes the estate or terminating income interest may become  
5 obligated to pay after the property is distributed.

6 **Sec. 13.38.510. Distribution to residuary and remainder beneficiaries.** (a)

7 Each beneficiary described in AS 13.38.500(4) is entitled to receive a portion of the  
8 net income equal to the beneficiary's fractional interest in undistributed principal  
9 assets, using values as of the distribution date. If a fiduciary makes more than one  
10 distribution of assets to beneficiaries to whom this section applies, each beneficiary,  
11 including one who does not receive part of the distribution, is entitled, as of each  
12 distribution date, to the net income the fiduciary has received after the date of death or  
13 terminating event or earlier distribution date but has not distributed as of the current  
14 distribution date.

15 (b) In determining a beneficiary's share of net income, the following rules  
16 apply:

17 (1) the beneficiary is entitled to receive a portion of the net income  
18 equal to the beneficiary's fractional interest in the undistributed principal assets  
19 immediately before the distribution date, including assets that later may be sold or  
20 applied to meet principal obligations;

21 (2) the beneficiary's fractional interest in the undistributed principal  
22 assets shall be calculated without regard to property specifically given to a beneficiary  
23 and property required to pay pecuniary amounts;

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

27 (c) If a fiduciary does not distribute all of the collected but undistributed net  
28 income to each person as of a distribution date, the fiduciary shall maintain  
29 appropriate records showing the interest of each beneficiary in that net income.

30 (d) To the extent that the fiduciary considers it appropriate, if this section  
31 applies to the income from an asset, the fiduciary may apply the rules in this section to

1 net gain or loss from the disposition of a principal asset realized after the date of death  
2 or terminating event or an earlier distribution date.

3 (e) For the purposes of this section, the distribution date may be the date as of  
4 which the fiduciary calculates the value of the assets if that date is reasonably near the  
5 date on which assets are actually distributed.

6 **Article 5. Apportionment at Beginning and End of Income Interest.**

7 **Sec. 13.38.550. When right to income begins and ends.** (a) An income  
8 beneficiary is entitled to net income from the date on which the income interest  
9 begins. An income interest begins

10 (1) on the date specified in the governing instrument; or

11 (2) if a date is not specified, on the date an asset becomes subject to a  
12 trust or successive income interest.

13 (b) An asset becomes subject to a trust

14 (1) on the date it is transferred to the trust, in the case of an asset that is  
15 transferred to a trust during the transferor's life;

16 (2) on the date of a testator's death, in the case of an asset that becomes  
17 subject to a trust by reason of a will, even if there is an intervening period of  
18 administration of the testator's estate; or

19 (3) on the date of an individual's death, in the case of an asset that is  
20 transferred to a fiduciary by a third party because of the individual's death.

21 (c) An asset becomes subject to a successive income interest on the day after  
22 the preceding income interest ends, as determined under (d) of this section, even if  
23 there is an intervening period of administration to wind up the preceding income  
24 interest.

25 (d) An income interest ends on

26 (1) the day before an income beneficiary dies or another terminating  
27 event occurs; or

28 (2) the last day of a period during which there is not a beneficiary to  
29 whom a trustee may distribute income.

30 **Sec. 13.38.560. Apportionment of receipts and disbursements when**  
31 **decedent dies or income interest begins.** (a) Unless AS 13.38.500(1) applies, a

1 trustee shall allocate an income receipt or disbursement to principal if its due date  
2 occurs before

3 (1) a decedent dies, in the case of an estate; or

4 (2) an income interest begins, in the case of a trust or successive  
5 income interest.

6 (b) A trustee shall allocate an income receipt or disbursement to income if its  
7 due date occurs on or after the date on which a decedent dies or an income interest  
8 begins and its due date is periodic. An income receipt or disbursement shall be treated  
9 as accruing from day to day if its due date is not periodic or it does not have a due  
10 date. The portion of the receipt or disbursement accruing before the date on which a  
11 decedent dies or an income interest begins shall be allocated to principal, and the  
12 balance shall be allocated to income.

13 (c) An item of income or an obligation is due on the date the payor is required  
14 to make a payment. If a payment date is not stated, there is not a due date for the  
15 purposes of this chapter. Distributions to shareholders or other owners from an entity  
16 to which AS 13.38.600 applies are considered to be due on the date fixed by the entity  
17 for determining who is entitled to receive the distribution or, if a date is not fixed, on  
18 the declaration date for the distribution. A due date is periodic for receipts or  
19 disbursements that must be paid at regular intervals under a lease or an obligation to  
20 pay interest or if an entity customarily makes distributions at regular intervals.

21 **Sec. 13.38.570. Apportionment when income interest ends.** (a) When a  
22 mandatory income interest ends, the trustee shall pay to a mandatory income  
23 beneficiary who survives that date, or the estate of a deceased mandatory income  
24 beneficiary whose death causes the interest to end, the beneficiary's share of the  
25 undistributed income that is not disposed of under the governing instrument unless the  
26 beneficiary has an unqualified power to revoke more than five percent of the trust  
27 immediately before the income interest ends. In the case of the beneficiary who has an  
28 unqualified power to revoke more than five percent of the trust immediately before the  
29 income interest ends, the undistributed income from the portion of the trust that may  
30 be revoked shall be added to principal.

31 (b) When a trustee's obligation to pay a fixed annuity or a fixed fraction of the

1 value of the trust's assets ends, the trustee shall prorate the final payment if and to the  
2 extent required by applicable law to accomplish a purpose of the trust or its settlor or  
3 testator relating to income, gift, estate, or other tax requirements.

4 (c) In this section, "undistributed income" means net income received before  
5 the date on which an income interest ends, but does not include an item of income or  
6 expense that is due or accrued or net income that has been added or is required to be  
7 added to principal under the governing instrument.

8 **Article 6. Allocation of Receipts during Administration of Trust.**

9 **Sec. 13.38.600. Character of receipts.** (a) Except as otherwise provided in  
10 this section, a trustee shall allocate to income money received from an entity,  
11 including reinvested cash dividends.

12 (b) A trustee shall allocate the following receipts from an entity to principal:

13 (1) property other than money excluding reinvested cash dividends;

14 (2) money received in one distribution or a series of related  
15 distributions in exchange for part or all of a trust's interest in the entity;

16 (3) money received in total or partial liquidation of the entity;

17 (4) money received from an entity that is a regulated investment  
18 company or a real estate investment trust if the money distributed is a short-term or  
19 long-term capital gain dividend for federal income tax purposes.

20 (c) Money is received in partial liquidation

21 (1) to the extent that the entity, at or near the time of a distribution,  
22 indicates that it is a distribution in partial liquidation; or

23 (2) if the total amount of money and property received in a distribution  
24 or series of related distributions is greater than 20 percent of the entity's gross assets,  
25 as shown by the entity's year-end financial statements immediately preceding the  
26 initial receipt.

27 (d) Money is not received in partial liquidation, and it may not be taken into  
28 account under (c)(2) of this section, to the extent that it does not exceed the amount of  
29 income tax that a trustee or beneficiary must pay on taxable income of the entity that  
30 distributes the money.

31 (e) A trustee may rely upon a statement made by an entity about the source or

1 character of a distribution if the statement is made at or near the time of distribution by  
2 the entity's board of directors or other person or group of persons authorized to  
3 exercise powers to pay money or transfer property comparable to those of a  
4 corporation's board of directors.

5 (f) In this section, "entity" means a corporation, partnership, limited liability  
6 company, regulated investment company, real estate investment trust, common trust  
7 fund, or another organization in which a trustee has an interest, but does not include

- 8 (1) a trust or estate to which AS 13.38.610 applies;
- 9 (2) a business or activity to which AS 13.38.620 applies;
- 10 (3) a payment to which AS 13.38.690 applies; or
- 11 (4) an asset-backed security to which AS 13.38.750 applies.

12 **Sec. 13.38.610. Distribution from trust or estate.** (a) A trustee shall  
13 allocate to income an amount received as a distribution of income from a trust or an  
14 estate in which the trust has an interest other than a purchased interest.

15 (b) A trustee shall allocate to principal an amount received as a distribution of  
16 principal from a trust or estate in which the trust has an interest other than a purchased  
17 interest.

18 (c) If a trustee purchases an interest in a trust that is an investment entity, or a  
19 decedent or donor transfers an interest in a trust that is an investment entity to a  
20 trustee, AS 13.38.600 or 13.38.750 applies to a receipt from the trust.

21 **Sec. 13.38.620. Business and other activities conducted by trustee.** (a) If a  
22 trustee that conducts a business or other activity determines that it is in the best  
23 interest of all the beneficiaries to account separately for the business or other activity  
24 instead of accounting for it as part of the trust's general accounting records, the trustee  
25 may maintain separate accounting records for the transactions of the business or other  
26 activity, whether or not the assets of the business or other activity are segregated from  
27 other trust assets.

28 (b) A trustee who accounts separately for a business or other activity may  
29 determine the extent to which

- 30 (1) its net cash receipts are retained for working capital, the acquisition  
31 or replacement of fixed assets, and other reasonably foreseeable needs of the business

1 or activity; and

2 (2) the remaining net cash receipts are accounted for as principal or  
3 income in the trust's general accounting records.

4 (c) If a trustee sells assets of the business or other activity, other than in the  
5 ordinary course of the business or activity, the trustee shall account for the net amount  
6 received as principal in the trust's general accounting records to the extent the trustee  
7 determines that the amount received is not required any longer in the conduct of the  
8 business.

9 (d) Activities for which a trustee may maintain separate accounting records  
10 include

11 (1) retail, manufacturing, service, and other traditional business  
12 activities;

13 (2) farming;

14 (3) raising and selling livestock and other animals;

15 (4) management of rental properties;

16 (5) extraction of minerals and other natural resources;

17 (6) timber operations; and

18 (7) activities to which AS 13.38.740 applies.

19 **Sec. 13.38.630. Principal receipts.** A trustee shall allocate to principal any of  
20 the following:

21 (1) to the extent not allocated to income under this chapter, assets  
22 received from

23 (A) a transferor during the transferor's lifetime;

24 (B) a decedent's estate;

25 (C) a trust with a terminating income interest; or

26 (D) a payor under a contract naming the trust or its trustee as  
27 beneficiary;

28 (2) money or other property received from a principal asset's sale,  
29 exchange, liquidation, or change in form, including realized profit subject to  
30 AS 13.38.600 -13.38.750;

31 (3) amounts recovered from third parties to reimburse the trust because

1 of disbursements described in AS 13.38.810(a)(8) or for other reasons, to the extent  
2 not based on the loss of income, except that a separate award made for the loss of  
3 income with respect to an accounting period during which a current income  
4 beneficiary had a mandatory income interest is income;

5 (4) net income received in an accounting period during which there is  
6 not a beneficiary to whom a trustee may or must distribute income;

7 (5) other receipts as provided in AS 13.38.680 - 13.38.750.

8 **Sec. 13.38.640. Rental property.** (a) To the extent that a trustee accounts for  
9 receipts from rental property under this section, the trustee shall allocate an amount  
10 received as rent of real or personal property to income, including an amount received  
11 for cancellation or renewal of a lease.

12 (b) An amount received as a refundable deposit, including a security deposit  
13 or a deposit that is to be applied as rent for future periods,

14 (1) shall be added to principal;

15 (2) shall be held subject to the terms of the lease; and

16 (3) is not available for distribution to a beneficiary until the trustee's  
17 contractual obligations have been satisfied with respect to that amount.

18 **Sec. 13.38.650. Obligation to pay money.** (a) An amount received as  
19 interest, whether determined at a fixed, variable, or floating rate, on an obligation to  
20 pay money to the trustee, including an amount received as consideration for prepaying  
21 principal, shall be allocated to income without any provision for amortization of  
22 premium.

23 (b) A trustee shall allocate to principal an amount received from the sale,  
24 redemption, or other disposition of an obligation to pay money to the trustee more than  
25 one year after it is purchased or acquired by the trustee, including an obligation if the  
26 purchase price or value of the obligation when it is acquired is less than its value at  
27 maturity. If the obligation matures within one year after it is purchased or acquired by  
28 the trustee, an amount received in excess of its purchase price or its value when  
29 acquired by the trust shall be allocated to income.

30 (c) This section does not apply to an obligation to which AS 13.38.690,  
31 13.38.700, 13.38.710, 13.38.720, 13.38.730, 13.38.740, or 13.38.750 applies.

1           **Sec. 13.38.660. Insurance policies and similar contracts.** (a) Except as  
2 otherwise provided in (b) or (c) of this section, a trustee shall allocate to principal the  
3 proceeds of a life insurance policy or other contract in which the trust or its trustee is  
4 named as beneficiary, including a contract that insures the trust or its trustee against  
5 loss for damage to, destruction of, or loss of title to a trust asset. If the premiums on  
6 the policy or contract are paid from income, the trustee shall allocate dividends on the  
7 policy or contract to income. If the premiums on the policy or contract are paid from  
8 principal, the trustee shall allocate dividends on the policy or contract to principal.

9           (b) Except as provided in (c) of this section, a trustee shall allocate to income  
10 proceeds of a contract that insures the trustee against

11                   (1) loss of occupancy or other use by an income beneficiary;

12                   (2) loss of income; or

13                   (3) subject to AS 13.38.620, loss of profits from a business.

14           (c) This section does not apply to a contract to which AS 13.38.690 applies.

15           **Sec. 13.38.670. Special rules for charitable remainder unitrusts.**

16 Notwithstanding the other provisions of this chapter, if a charitable remainder unitrust,  
17 as defined in 26 U.S.C. 664 (Internal Revenue Code), owns an obligation described in  
18 (2) of this section, the following rules apply, unless varied by the governing  
19 instrument:

20                   (1) an obligation for the payment of money is principal at its inventory  
21 value except as provided in (2) of this section; the trustee may not make a provision  
22 for amortization of a premium or for accumulation for discount;

23                   (2) except to the extent otherwise provided in the governing  
24 instrument, an increase in the value of the following above inventory value is  
25 distributable as income:

26                           (A) a zero coupon bond;

27                           (B) an annuity contract before annuitization;

28                           (C) a life insurance contract before the death of the insured;

29                           (D) an interest in a common trust fund; in this subparagraph,  
30 "common trust fund" has the meaning given in 26 U.S.C. 584 (Internal  
31 Revenue Code);

1 (E) an interest in a limited liability company, limited liability  
2 partnership, or limited partnership; and

3 (F) another obligation for the payment of money if the money  
4 is payable at a future time under a fixed, variable, or discretionary schedule of  
5 appreciation and if the payment exceeds the price at which the obligation was  
6 issued;

7 (3) the increase in value of the obligations described in (2) of this  
8 section is distributable to the beneficiary who was the income beneficiary at the time  
9 of the increase; the increase is distributable from the first cash available from the  
10 principal or, if cash is not available from the principal, when cash is first available  
11 from the principal due to a sale, a redemption, or another disposition; when an  
12 unrealized increase is distributed as income from principal, the principal shall be  
13 reimbursed when the increase is realized;

14 (4) the increase in value of an obligation described in (2) of this  
15 section is not available for distribution unless the trustee receives cash on account of  
16 the obligation;

17 (5) notwithstanding a provision in this section to the contrary, a  
18 distribution from a partnership or limited liability company attributable to the cash  
19 flow or income derived from operations regularly carried on by the partnership or  
20 limited liability company is income, except to the extent otherwise provided in the  
21 governing instrument.

22 **Sec. 13.38.680. Insubstantial allocations not required.** If a trustee  
23 determines that an allocation between principal and income required by AS 13.38.690,  
24 13.38.700, 13.38.710, 13.38.720, or 13.38.750 is insubstantial, the trustee may allocate  
25 the entire amount to principal unless one of the circumstances described in  
26 AS 13.38.210(c) applies to the allocation. This power may be exercised by a co-  
27 trustee in the circumstances described in AS 13.38.210(d) and may be released for the  
28 reasons and in the manner described in AS 13.38.210(e). An allocation is presumed to  
29 be insubstantial if

30 (1) the amount of the allocation would increase or decrease net income  
31 in an accounting period, as determined before the allocation, by less than five percent;

1 or

2 (2) the value of the asset producing the receipt for which the allocation  
3 would be made is less than five percent of the total value of the trust's assets at the  
4 beginning of the accounting period.

5 **Sec. 13.38.690. Retirement benefits, individual retirement accounts,**  
6 **deferred compensation, annuities, and similar payments.** (a) The trustee shall  
7 allocate to income the greater of the portion of a payment characterized by the payor  
8 as interest or a dividend, as a remittance in place of interest or a dividend, or as  
9 imputed interest for federal income tax purposes. The balance of the payment shall be  
10 allocated to principal.

11 (b) If a part of a payment under a contract calling for equal installments over a  
12 fixed period of time is not allocable to income under the provisions of (a) of this  
13 section, the difference between the trust's acquisition value of the contract and the total  
14 expected return shall be considered to be interest. The trustee shall allocate to income  
15 the portion of each payment equivalent to interest on the then unpaid principal balance  
16 at the rate specified in the contract or at a rate necessary to amortize the difference  
17 between the expected return and the acquisition value, where that rate is readily  
18 ascertainable by the trustee.

19 (c) If there is not a portion of a payment from a separate fund held exclusively  
20 for the benefit of the trust that is allocable to income under (a) or (b) of this section,  
21 but the internal net income of the fund determined as if the fund were a separate trust  
22 subject to AS 13.38.500 - 13.38.860 is readily ascertainable by the trustee, the portion  
23 of the payment equal to the then undistributed net income of the fund realized since  
24 the trust acquired its interest in the fund is considered to be a distribution of income  
25 and shall be allocated to the trust income account. The balance of the payment  
26 described in this subsection shall be allocated to principal.

27 (d) A trustee shall allocate 10 percent of the part of the payment that is  
28 required to be made during the accounting period to income and the balance to  
29 principal if there is not a part of the payment that is allocable to income under (a) - (c)  
30 of this section and all or part of the payment is required to be made. The trustee shall  
31 allocate the entire payment to principal if a part of a payment is not required to be

1 made or the payment received is the entire amount to which the trustee is entitled. In  
2 this subsection, a payment is not "required to be made" to the extent that it is made  
3 because the trustee exercises a right of withdrawal.

4 (e) If, to obtain a federal estate or gift tax marital deduction for a trust, the  
5 trustee must allocate more of a payment to income than provided for by this section,  
6 the trustee shall allocate the additional amount necessary to obtain the marital  
7 deduction to income.

8 (f) This section does not apply to payments to which AS 13.38.700 applies.

9 (g) In this section, "payment" means a payment that a trustee may receive over  
10 a fixed period of time or during the life of one or more individuals because of services  
11 rendered or property transferred to the payor in exchange for future payments, and  
12 includes

13 (1) a payment made in money or property from the payor's general  
14 assets or from a separate fund created by the payor or another person;

15 (2) a payment on or from

16 (A) an installment contract or note;

17 (B) a private or commercial annuity;

18 (C) a deferred compensation agreement;

19 (D) an employee death benefit;

20 (E) an individual retirement account; or

21 (F) a pension plan, profit-sharing plan, stock plan, bonus plan,  
22 or stock-ownership plan.

23 **Sec. 13.38.700. Liquidating asset.** (a) A trustee shall allocate 10 percent of  
24 the receipts from a liquidating asset to income and the balance to principal.

25 (b) In this section, "liquidating asset"

26 (1) means

27 (A) an asset the value of which will diminish or terminate  
28 because the asset is expected to produce receipts for a period of limited  
29 duration; or

30 (B) a leasehold, patent, copyright, royalty right, and right to  
31 receive payments during a period of more than one year under an arrangement

1 that does not provide for the payment of interest on the unpaid balance;

2 (2) does not include

3 (A) an obligation subject to AS 13.38.670;

4 (B) a payment subject to AS 13.38.690;

5 (C) resources subject to AS 13.38.710;

6 (D) timber subject to AS 13.38.720;

7 (E) an activity subject to AS 13.38.740;

8 (F) an asset subject to AS 13.38.750; or

9 (G) an asset for which the trustee establishes a reserve for

10 depreciation under AS 13.38.830.

11 **Sec. 13.38.710. Minerals, water, and other natural resources.** (a) To the  
12 extent that a trustee accounts for receipts from an interest in minerals or other natural  
13 resources under this section, the trustee shall allocate them as follows:

14 (1) if received as nominal delay rent or nominal annual rent on a lease,  
15 a receipt shall be allocated to income;

16 (2) if received from a production payment, a receipt shall be allocated  
17 to income if and to the extent that the agreement creating the production payment  
18 provides a factor for interest or its equivalent; the balance shall be allocated to  
19 principal;

20 (3) if an amount received as a royalty, shut-in-well payment, take-or-  
21 pay payment, bonus, or delay rental is more than nominal, 90 percent shall be  
22 allocated to principal, and the balance shall be allocated to income;

23 (4) if an amount is received from a working interest or any other  
24 interest not provided for in (1) - (3) of this subsection, 90 percent of the net amount  
25 received shall be allocated to principal, and the balance shall be allocated to income.

26 (b) An amount received on account of an interest in renewable water shall be  
27 allocated to income. An amount received on account of an interest in nonrenewable  
28 water shall be allocated as follows:

29 (1) 90 percent of the amount shall be allocated to principal; and

30 (2) the balance shall be allocated to income.

31 (c) This chapter applies whether or not a decedent or donor was extracting

1 minerals, water, or other natural resources before the interest became subject to the  
2 trust.

3 **Sec. 13.38.720. Timber.** (a) To the extent that a trustee accounts for receipts  
4 from the sale of timber and related products under this section, the trustee shall  
5 allocate the net receipts

6 (1) to income, to the extent that the amount of timber removed from  
7 the land does not exceed the rate of growth of the timber during the accounting periods  
8 in which a beneficiary has a mandatory income interest;

9 (2) to principal, to the extent that the amount of timber removed from  
10 the land exceeds the rate of growth of the timber, or the net receipts are from the sale  
11 of standing timber;

12 (3) between income and principal, by determining the amount of  
13 timber removed from the land under the lease or contract and applying the rules in (1)  
14 and (2) of this subsection if the net receipts are from the lease of timberland or a  
15 contract to cut timber from land owned by a trust;

16 (4) to principal to the extent that advance payments, bonuses, and other  
17 payments are not allocated under (1) - (3) of this subsection.

18 (b) In determining net receipts to be allocated under (a) of this section, a  
19 trustee shall deduct and transfer to principal a reasonable amount for depletion.

20 (c) This chapter applies whether or not a decedent or transferor was harvesting  
21 timber from the property before it became subject to the trust.

22 **Sec. 13.38.730. Property not productive of income.** (a) If a federal estate or  
23 gift tax marital deduction is allowed for all or part of a trust whose income is required  
24 to be paid to the settlor's or testator's spouse and whose assets consist substantially of  
25 property that does not provide the spouse with sufficient income from or use of the  
26 trust assets, and if the amounts that the trustee transfers from principal to income  
27 under AS 13.38.210 and that the trustee distributes to the spouse from principal under  
28 the governing instrument are insufficient to provide the spouse with the beneficial  
29 enjoyment required to obtain the marital deduction, the spouse may require the trustee  
30 to make property productive of income, convert property within a reasonable time, or  
31 exercise the power conferred by AS 13.38.210(a). The trustee may decide which

1 action or combination of actions to take.

2 (b) In cases not governed by (a) of this section, proceeds from the sale or other  
3 disposition of an asset are principal without regard to the amount of income the asset  
4 produces during any accounting period.

5 **Sec. 13.38.740. Derivatives and options.** (a) To the extent that a trustee  
6 does not account under AS 13.38.620 for transactions in derivatives, the trustee shall  
7 allocate receipts from and disbursements made in connection with those transactions  
8 to principal.

9 (b) If a trustee grants an option to buy property from the trust, whether or not  
10 the trust owns the property when the option is granted, grants an option that permits  
11 another person to sell property to the trust, or acquires an option to buy property for  
12 the trust or an option to sell an asset owned by the trust, and the trustee or other owner  
13 of the asset is required to deliver the asset if the option is exercised, an amount  
14 received for granting the option shall be allocated to principal. An amount paid to  
15 acquire the option shall be paid from principal. A gain or loss realized upon the  
16 exercise of an option, including an option granted to a settlor or testator of the trust for  
17 services rendered, shall be allocated to principal.

18 (c) In this section, "derivative" means a contract or financial instrument or a  
19 combination of contracts and financial instruments that gives a trust the right or  
20 obligation to participate in some or all changes in the price of a tangible or intangible  
21 asset or group of assets, or changes in a rate, an index of prices or rates, or another  
22 market indicator for an asset or a group of assets.

23 **Sec. 13.38.750. Asset-backed securities.** (a) If a trust receives a payment  
24 from interest or other current return and from other proceeds of the collateral financial  
25 assets, the trustee shall allocate the portion of the payment that the payor identifies as  
26 being from interest or other current return to income, and the trustee shall allocate the  
27 balance of the payment to principal.

28 (b) If a trust receives one or more payments in exchange for the trust's entire  
29 interest in an asset-backed security in one accounting period, the trustee shall allocate  
30 the payments to principal. If a payment is one of a series of payments that will result  
31 in the liquidation of the trust's interest in the security over more than one accounting

1 period, the trustee shall allocate 10 percent of the payment to income and the balance  
2 to principal.

3 (c) In this section, "asset-backed security"

4 (1) means an asset whose value is based on the right it gives the owner  
5 to receive distributions from the proceeds of financial assets that provide collateral for  
6 the security;

7 (2) includes an asset that gives the owner the right to receive from the  
8 collateral financial assets only the interest or other current return or only the proceeds  
9 other than interest or current return;

10 (3) does not include an asset to which AS 13.38.600 or 13.38.690  
11 applies.

12 **Article 7. Allocation of Disbursements During Administration of Trust.**

13 **Sec. 13.38.800. Mandatory disbursements from income.** A trustee shall  
14 make the following disbursements from income:

15 (1) interest, except interest on taxes described in AS 13.38.810(a)(7);

16 (2) ordinary repairs;

17 (3) real estate and other regularly recurring taxes assessed against  
18 principal;

19 (4) recurring premiums on fire or other insurance covering the loss of a  
20 principal asset or the loss of income from or use of the asset.

21 **Sec. 13.38.810. Mandatory disbursements from principal.** (a) A trustee  
22 shall make the following disbursements from principal:

23 (1) extraordinary expenses incurred in connection with the  
24 administration, management, or preservation of trust property and the distribution of  
25 income;

26 (2) extraordinary repairs;

27 (3) compensation for legal services to the trustee;

28 (4) expenses in connection with accountings and judicial or other  
29 proceedings, including proceedings to construe, modify, or reform the trust or to  
30 protect the trust or its property;

31 (5) payments on the principal of a trust debt;

1 (6) premiums paid on a policy of insurance not described in  
2 AS 13.38.800(4) if the trust is the owner and beneficiary;

3 (7) estate, inheritance, and other transfer taxes, including interest and  
4 penalties, apportioned to the trust;

5 (8) disbursements related to environmental matters, including

6 (A) reclamation;

7 (B) assessing environmental conditions;

8 (C) remedying and removing environmental contamination;

9 (D) monitoring remedial activities and the release of  
10 substances;

11 (E) preventing future releases of substances;

12 (F) collecting amounts from persons liable or potentially liable  
13 for the costs of those activities;

14 (G) penalties imposed under environmental statutes or  
15 regulations and other payments made to comply with those statutes or  
16 regulations;

17 (H) statutory or common law claims by third parties;

18 (I) defending claims based on environmental matters.

19 (b) If a principal asset is encumbered with an obligation that requires income  
20 from that asset to be paid directly to the creditor, the trustee shall transfer from  
21 principal to income an amount equal to the income paid to the creditor in reduction of  
22 the principal balance of the obligation.

23 **Sec. 13.38.820. Discretionary allocation of disbursements.** Subject to  
24 AS 13.38.800 and 13.38.810, a trustee may, in the trustee's discretion, allocate to  
25 income or principal or partly to each ordinary expenses incurred in connection with  
26 the administration, management, or preservation of trust property and the distribution  
27 of income, including the compensation of the trustee and of a person providing  
28 investment advisory, custodial, or income tax return preparation services to the trustee.

29 **Sec. 13.38.830. Transfers from income to principal for depreciation.** (a)  
30 A trustee may transfer to principal a reasonable amount of the net cash receipts from a  
31 principal asset that is subject to depreciation. However, a trustee may not transfer any

1 amount for depreciation

2 (1) of that portion of real property used or available for use by a  
3 beneficiary as a residence or of tangible personal property held or made available for  
4 the personal use or enjoyment of a beneficiary;

5 (2) during the administration of a decedent's estate; or

6 (3) under this section if the trustee is accounting under AS 13.38.620  
7 for the business or activity in which the asset is used.

8 (b) An amount transferred to principal is not required to be held as a separate  
9 fund.

10 (c) In this section, "depreciation" means a reduction in value due to wear, tear,  
11 decay, corrosion, or gradual obsolescence of a fixed asset having a useful life of more  
12 than one year.

13 **Sec. 13.38.840. Transfers from income to reimburse principal.** (a) A  
14 trustee may transfer an appropriate amount from income to principal in one or more  
15 accounting periods to reimburse principal or to provide a reserve for future  
16 disbursements if the trustee makes or expects to make a disbursement from principal  
17 that is allocable to income under AS 13.38.800 or 13.38.820 and that is paid from  
18 principal because it is unusually large, or is made to prepare property for rental,  
19 including tenant allowances, leasehold improvements, and broker's commissions.

20 (b) If the asset whose ownership gives rise to the disbursements becomes  
21 subject to a successive income interest after an income interest ends, a trustee may  
22 continue to transfer amounts from income to principal as provided in (a) of this  
23 section.

24 (c) This section does not apply to the extent the trustee has been or expects to  
25 be reimbursed by a third party.

26 **Sec. 13.38.850. Income taxes.** (a) A tax required to be paid by a trustee  
27 based on receipts allocated to income shall be paid from income.

28 (b) A tax required to be paid by a trustee based on receipts allocated to  
29 principal shall be paid from principal, even if the tax is called an income tax by the  
30 taxing authority.

31 (c) A tax required to be paid by a trustee on the trust's share of an entity's

1 taxable income shall be paid proportionately from

2 (1) income, to the extent that receipts from the entity are allocated to  
3 income; and

4 (2) principal, to the extent that

5 (A) receipts from the entity are allocated to principal; and

6 (B) the trust's share of the entity's taxable income exceeds the  
7 total receipts described in (1) of this subsection and (A) of this paragraph.

8 (d) For the purposes of this section, receipts allocated to principal or income  
9 shall be reduced by the amount distributed to a beneficiary from principal or income  
10 for which the trust receives a deduction in calculating the tax.

11 **Sec. 13.38.860. Adjustments between principal and income because of**  
12 **taxes.** A trustee may make adjustments between principal and income to offset the  
13 shifting of economic interests or tax benefits between income beneficiaries and  
14 remainder beneficiaries that arise from

15 (1) an election or decision that the trustee makes regarding tax matters;

16 (2) an income tax or any other tax that is imposed on the trustee or a  
17 beneficiary as a result of a transaction involving the trust or distribution from the trust;  
18 or

19 (3) the ownership by a trust of an interest in an entity whose taxable  
20 income, whether or not distributed, is includable in the taxable income of the trust or a  
21 beneficiary.

#### 22 **Article 8. General Provisions.**

23 **Sec. 13.38.900. Not applicable to mental health trust.** This chapter does not  
24 apply to the trust established under the Alaska Mental Health Enabling Act of 1956,  
25 P.L. 84-830, 70 Stat. 709.

26 **Sec. 13.38.910. Uniformity of application and construction.** In applying  
27 and construing this chapter, consideration shall be given to the need to promote  
28 uniformity of the law with respect to its subject matter among states that enact it.

29 **Sec. 13.38.980. Definitions.** In this chapter, unless the context clearly  
30 indicates otherwise,

31 (1) "accounting period" means a calendar year, unless another 12-

1 month period is selected by a fiduciary, and includes a portion of a calendar year or  
2 other 12-month period that begins when an income interest begins or ends when an  
3 income interest ends;

4 (2) "beneficiary" includes, in the case of

5 (A) a decedent's estate, an heir, legatee, or devisee; and

6 (B) a trust, an income beneficiary and a remainder beneficiary;

7 (3) "fiduciary" means a personal representative or a trustee;

8 (4) "income" means money or property that a fiduciary receives as  
9 current return from a principal asset, and includes a portion of receipts from a sale,  
10 exchange, or liquidation of a principal asset, to the extent provided in AS 13.38.600 -  
11 13.38.750;

12 (5) "income beneficiary" means a person to whom net income of a  
13 trust is or may be payable;

14 (6) "income interest" means the right of an income beneficiary to  
15 receive all or part of net income, whether the governing instrument requires it to be  
16 distributed or authorizes it to be distributed in the trustee's discretion;

17 (7) "mandatory income interest" means the right of an income  
18 beneficiary to receive net income that the governing instrument requires the fiduciary  
19 to distribute;

20 (8) "net income" means the total receipts allocated to income during an  
21 accounting period, minus disbursements made from income during the period, and  
22 plus or minus transfers under this chapter to or from income during the period;

23 (9) "person" means an individual, a corporation, a business trust, an  
24 estate, a trust, a partnership, a limited liability company, an association, a joint  
25 venture, a government, a governmental subdivision, an agency or instrumentality, a  
26 public corporation, or another legal or commercial entity;

27 (10) "principal" means property held in trust for distribution to a  
28 remainder beneficiary when the trust terminates, or property held in trust in perpetuity;

29 (11) "remainder beneficiary" means a person entitled to receive  
30 principal when an income interest ends;

31 (12) "sui juris beneficiary" includes

- 1 (A) a court-appointed guardian of an incapacitated beneficiary;  
2 (B) an agent for an incompetent beneficiary; and  
3 (C) a court-appointed guardian of a minor beneficiary's estate;  
4 (13) "trust" includes a revocable trust, an irrevocable trust, and a legal  
5 life estate arrangement;  
6 (14) "trustee" includes an original, additional, or successor trustee,  
7 whether or not appointed or confirmed by a court;  
8 (15) "unitrust" means a trust from which a fixed percentage of the net  
9 fair market value of the trust's assets, valued annually, is paid not less often than  
10 annually to a beneficiary.

11 **Sec. 13.38.990. Short title.** This chapter may be cited as the Alaska Principal  
12 and Income Act.

13 \* **Sec. 3.** AS 37.14.031(d) is amended to read:

14 (d) The authority shall adopt regulations providing for the determination  
15 of [PROVISIONS OF AS 13.38 APPLY TO DETERMINE] amounts attributable to  
16 [THE] principal under (b)(2) of this section. The regulations must provide for the  
17 allocation between principal and income of money received from the  
18 management of mental health trust land, and the manner of allocation must be in  
19 the long-term best interest of the trust and its beneficiaries.

20 \* **Sec. 4.** AS 13.16.550; AS 13.38.010, 13.38.020, 13.38.030, 13.38.040, 13.38.050,  
21 13.38.060, 13.38.070, 13.38.080, 13.38.090, 13.38.100, 13.38.110, 13.38.120, 13.38.130, and  
22 13.38.140 are repealed.

23 \* **Sec. 5.** The uncodified law of the State of Alaska is amended by adding a new section to  
24 read:

25 **APPLICABILITY.** AS 13.38.200 - 13.38.990, enacted by sec. 2 of this Act, apply,  
26 except as otherwise expressly provided in the governing instrument, and except as provided  
27 by AS 13.38.900, enacted by sec. 2 of this Act, to a trust existing on or after the effective date  
28 of this Act, and to the estate of a decedent who dies on or after the effective date of this Act.

29 \* **Sec. 6.** This Act takes effect September 1, 2003.

# ALASKA STATE SENATE



Session:  
State Capitol  
Juneau, Alaska 99801-1182  
(907) 465-2327  
(907) 465-5241 Fax

Interim:  
119 N. Cushman, Suite 201  
Fairbanks, Alaska 99701  
(907) 456-8161  
Senator\_Ralph\_Seekins@legis.state.ak.us

**Senator Ralph Seekins**  
District D

## MEMORANDUM

Date: April 23, 2003

To: Office of Representative McGuire

From: Senator Ralph Seekins

A handwritten signature in black ink, appearing to read "R. Seekins" or similar, written over the "From:" line.

Re: Request for Hearing of SB 87

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Attached please find Senate Bill 87 along with the corresponding sponsor statement and supporting documentation.

This Bill essentially updates the Uniform Principal and Income Act to the 1997 version. It not only enjoys industry support but also bi-partisan support in the Senate passing out on a 17 to 0 vote.

I respectfully request a hearing before your committee on this Bill at your earliest convenience. Thank you.

# ALASKA STATE SENATE



Session:  
State Capitol  
Juneau, Alaska 99801-1182  
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119 N. Cushman, Suite 201  
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**Senator Ralph Seekins**  
District D

## Senate Bill 87 Sponsor Statement

### Update of the Uniform Principal and Income Act

In 1984 the Alaska legislature adopted an early version of the Uniform Principal and Income Act (located in Statute 13.38). This Act provides rules for the determination of whether a trust's or estate's receipts should be considered income or principal. This distinction is often important because some beneficiaries may be entitled to income distributions, and others may be entitled to principal distributions. Senate Bill 87 updates the existing Statute to the most recent (1997) version of the Uniform Principal and Income Act.

The drafters of the 1997 Uniform Act have recognized that there is a conflict between income and principal beneficiaries, and this conflict creates pressures on the fiduciary. The income beneficiaries want the fiduciary to invest so as to maximize annual income. The principal beneficiaries want the fiduciary to invest for long term equity growth. As a result, a trustee attempting to satisfy both sets of beneficiaries will have to compromise with respect to the choice of investments. Consequently, the total return of the trust will suffer. Two techniques have been adopted to avoid the need for such a compromise. These techniques allow the trustee to choose investment approaches which will maximize the total investment return of the trust.

The first technique is provided by Article 1 of Senate Bill 87, which gives the trustee the discretionary power to adjust. This power allows the trustee to reallocate receipts from income to principal, or vice versa, when the trustee determines that it is fair and reasonable to do so. The second technique is provided by Article 2 which allows the trustee to convert a trust to a unitrust. This is a trust which provides that a certain percentage of its assets—often 4%—will be distributed each year to the income beneficiary.

Both of the above techniques will allow the trustee to choose investment approaches which will maximize the total return. As a result, both the income beneficiary and the principal beneficiary will receive greater distributions. Further, the trustee will not be struggling with the conflict in investment approaches.

As of January 2003, thirty states have adopted the 1997 Uniform Principal and Income Act. Of these, twelve states have included the unitrust provisions. Senate Bill 87 follows the legislation enacted by Pennsylvania, which includes both techniques thereby enabling the trustee to maximize total returns. The State of Washington enacted this version in 2002. Georgia is presently considering it this year.

April 21, 2003

# The TRUST

Representative Lesil McGuire  
State Capital  
Juneau, Alaska 99801

The Alaska Mental Health Trust Authority

**Re: SB 87**

Dear Representative McGuire,

We have had Ron Lorenson, a former long time Department of Law attorney under contract to the Trust, review SB 87. He has suggested the following amendments to the bill to ensure that it does not conflict with the Mental Health Trust settlement.

A. At page 31, line 30, insert a new bill section to read:

\* **Sec. 3.** AS 37.14.031(d) is amended to read:

(d) The Alaska Mental Health Trust Authority shall adopt regulations providing for the determination of [PROVISIONS OF AS 13.38 APPLY TO DETERMINE] amounts attributable to the principal under (b)(2) of this section. The regulations shall provide for allocations between principal and income of money received from the management of mental health trust land in a manner that is in the long term best interest of the trust and its beneficiaries.

P Renumber remaining bill sections, accordingly.

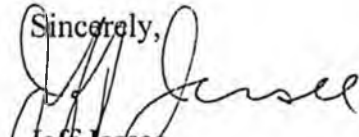
C. At page 32, amend the applicability provision set out at lines 4 - 7 to read:

APPLICABILITY. (a) AS 13.38.200 - 13.38.990, enacted by sec. 2 of this Act, apply, except as otherwise expressly provided in the governing instrument, to a trust existing on or after the effective date of this Act, and to the estate of a decedent who dies on or after the effective date of this Act.

(b) AS 13.38.200 - 13.38.990, enacted by sec. 2 of this Act, do not apply to the trust established under the Alaska Mental Health Enabling Act of 1956, P.L. 84-830, 70 Stat. 709.

We are also sharing these proposed amendments the bill sponsor, Senator Ralph Seekins, for his consideration. We have asked him to review these amendments and if he finds them acceptable to communicate that fact to you. Our own support for these amendments is contingent on Senator Seekins finding them acceptable.

Thank you for your consideration.

Sincerely,  
  
Jeff Jessee  
Executive Director

23-LS0366\Q  
Bannister  
4/25/03

HOUSE CS FOR SENATE BILL NO. 87( )  
IN THE LEGISLATURE OF THE STATE OF ALASKA  
TWENTY-THIRD LEGISLATURE - FIRST SESSION

BY

Offered:  
Referred:

Sponsor(s): SENATOR SEEKINS

A BILL

FOR AN ACT ENTITLED

1 "An Act relating to principal and income in the administration of trusts and decedents'  
2 estates and the mental health trust fund; adopting a version of the Uniform Principal  
3 and Income Act; and providing for an effective date."

4 BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF ALASKA:

5 \* Section 1. AS 13.36.335 is amended to read:

6 Sec. 13.36.335. Application of special distribution provisions. The asset  
7 distribution provisions of AS 13.16.540 - 13.16.550, 13.16.560, and AS 13.38.550(a)  
8 [AS 13.38.030(a)] apply to the administration of a revocable trust following the death  
9 of the settlor of the trust, unless the terms of the trust indicate a different intention.

10 \* Sec. 2. AS 13.38 is amended by adding new sections to read:

11 Article 1. Preliminary Provisions; Power to Adjust.

12 Sec. 13.38.200. Fiduciary duties; general principles. (a) In allocating  
13 receipts and disbursements to or between principal and income and with respect to any  
14 matter within the scope of this chapter, a fiduciary

1 (1) shall administer a trust or estate in accordance with the governing  
2 instrument, even if there is a different provision in this chapter;

3 (2) may administer a trust or estate by the exercise of a discretionary  
4 power of administration regarding a matter within the scope of this chapter given to  
5 the fiduciary by the governing instrument, even if the exercise of the power produces a  
6 result different from a result required or permitted by this chapter; an inference that  
7 the fiduciary has improperly exercised the discretionary power does not arise from the  
8 fact that the fiduciary has made an allocation contrary to a provision of this chapter;

9 (3) shall administer a trust or estate in accordance with this chapter if  
10 the governing instrument does not contain a different provision or does not give the  
11 fiduciary a discretionary power of administration regarding a matter within the scope  
12 of this chapter; and

13 (4) shall add a receipt or charge a disbursement to principal to the  
14 extent that the governing instrument and this chapter do not provide a rule for  
15 allocating the receipt or disbursement to or between principal and income.

16 (b) In exercising a discretionary power of administration regarding a matter  
17 within the scope of this chapter, whether granted by the governing instrument or this  
18 chapter, including AS 13.38.210 and 13.38.300 - 13.38.410, a fiduciary shall  
19 administer a trust or estate impartially based on what is fair and reasonable to all of the  
20 beneficiaries, except to the extent that the governing instrument clearly manifests an  
21 intention that the fiduciary shall or may favor one or more of the beneficiaries. A  
22 determination in accordance with this chapter is presumed to be fair and reasonable to  
23 all of the beneficiaries.

24 **Sec. 13.38.210. Trustee's power to adjust.** (a) Subject to (c) and (f) of this  
25 section, a trustee may adjust between principal and income by allocating an amount of  
26 income to principal or an amount of principal to income to the extent the trustee  
27 considers appropriate if

28 (1) the governing instrument describes what may or shall be distributed  
29 to a beneficiary by referring to the trust's income;

30 (2) the trustee determines, after applying the rules in AS 13.38.200(a),  
31 that the trustee is unable to comply with AS 13.38.200(b); and

1 (3) the trustee determines to follow an investment policy seeking a total return  
2 for the investments held by the trust, whether the return is to be derived from

3 (A) appreciation of capital;

4 (B) earnings and distributions from capital; or

5 (C) both (A) and (B) of this paragraph.

6 (b) In deciding whether and to what extent to exercise the power conferred by  
7 (a) of this section, a trustee may consider, among other things,

8 (1) the size of the trust;

9 (2) the nature and estimated duration of the trust;

10 (3) the liquidity and distribution requirements of the trust;

11 (4) the need for regular distributions and preservation and appreciation  
12 of capital;

13 (5) the expected tax consequences of an adjustment;

14 (6) the net amount allocated to income under the other sections of this  
15 chapter and the increase or decrease in the value of the principal assets, which the  
16 trustee may estimate as to assets for which market values are not readily available;

17 (7) the assets held in the trust; the extent to which the assets consist of  
18 financial assets, interests in closely held enterprises, tangible and intangible personal  
19 property, or real property; the extent to which an asset is used by a beneficiary; and  
20 whether an asset was purchased by the trustee or received from the settlor or testator;

21 (8) to the extent reasonably known to the trustee, the need of the  
22 beneficiaries for present and future distributions authorized or required by the  
23 governing instrument;

24 (9) whether and to what extent the governing instrument gives the  
25 trustee the power to invade principal or accumulate income or prohibits the trustee  
26 from invading principal or accumulating income, and the extent to which the trustee  
27 has exercised a power from time to time to invade principal or accumulate income;

28 (10) the intent of the settlor or testator; and

29 (11) the actual and anticipated effect of economic conditions on  
30 principal and income and the effects of inflation and deflation.

31 (c) A trustee may not make an adjustment under this section if

1 (1) the adjustment would diminish the income interest in a trust that  
2 requires all of the income to be paid at least annually to a spouse and for which a  
3 federal estate tax or gift tax marital deduction would be allowed, in whole or in part, if  
4 the trustee did not have the power to make the adjustment; the prohibition in this  
5 paragraph does not apply to a trust after the trustee determines that the marital  
6 deduction has not been claimed or has not been allowed;

7 (2) the adjustment would reduce the actuarial value of the income  
8 interest in a trust to which a person transfers property with the intent to qualify for a  
9 federal gift tax exclusion;

10 (3) the adjustment would change the amount payable to a beneficiary  
11 as a fixed annuity or a fixed fraction of the value of the trust assets;

12 (4) the adjustment is from any amount that is permanently set aside for  
13 charitable purposes under the governing instrument and for which a federal estate or  
14 gift tax charitable deduction has been taken, unless both income and principal are  
15 permanently set aside for charitable purposes under the governing instrument;

16 (5) possessing or exercising the power to make an adjustment would  
17 cause an individual to be treated as the owner of all or part of the trust for federal  
18 income tax purposes, and the individual would not be treated as the owner if the  
19 trustee did not possess the power to make an adjustment;

20 (6) possessing or exercising the power to make an adjustment would  
21 cause all or part of the trust assets to be subject to federal estate or gift tax with respect  
22 to an individual, and the assets would not be subject to federal estate or gift tax with  
23 respect to the individual if the trustee did not possess the power to make an  
24 adjustment;

25 (7) the trustee is a beneficiary of the trust; or

26 (8) the trust has been converted to a unitrust under AS 13.38.300 -  
27 13.38.410.

28 (d) If (c)(5), (6), or (7) of this section applies to a trustee and there is more  
29 than one trustee, a co-trustee to whom the provision does not apply may make the  
30 adjustment unless the exercise of the power by the remaining trustee or trustees is  
31 prohibited by the governing instrument.

1 (e) A trustee may release the entire power conferred by (a) of this section, the  
2 power to adjust from income to principal, or the power to adjust from principal to  
3 income if the trustee is uncertain about whether possessing or exercising the power  
4 will cause a result described in (c)(1) - (6) of this section, or if the trustee determines  
5 that possessing or exercising the power will or may deprive the trust of a tax benefit or  
6 impose a tax burden not described in (c) of this section. The release may be  
7 permanent or for a specified period, including a period measured by the life of an  
8 individual.

9 (f) A governing instrument that limits the power of a trustee to make an  
10 adjustment between principal and income does not affect the application of this  
11 section unless it is clear from the governing instrument that it is intended to deny the  
12 trustee the power of adjustment conferred by (a) of this section.

13 **Sec. 13.38.220. Judicial control of discretionary powers.** (a) A court may  
14 not change a fiduciary's decision to exercise or not to exercise a discretionary power  
15 conferred by this chapter unless the court determines that the decision was an abuse of  
16 the fiduciary's discretion.

17 (b) If a court determines that a fiduciary has abused the fiduciary's discretion  
18 regarding a discretionary power conferred by this chapter, the remedy is to restore the  
19 income and remainder beneficiaries to the positions they would have occupied if the  
20 fiduciary had not abused the fiduciary's discretion, according to the following rules:

21 (1) to the extent that the abuse of discretion has not resulted in a  
22 distribution to a beneficiary or has resulted in a distribution that is too small, the court  
23 shall require the fiduciary to distribute from the trust an amount to the beneficiary that  
24 the court determines will restore the beneficiary, in whole or in part, to the  
25 beneficiary's appropriate position;

26 (2) to the extent that the abuse of discretion has resulted in a  
27 distribution to a beneficiary that is too large, the court shall restore the beneficiaries,  
28 the trust, or both, in whole or in part, to their appropriate positions by requiring the  
29 fiduciary to withhold an amount from one or more future distributions to the  
30 beneficiary who received the distribution that was too large or by requiring that  
31 beneficiary or that beneficiary's estate to return some or all of the distribution to the

1 trust, notwithstanding a spendthrift or similar provision;

2 (3) if the abuse of discretion concerns the power to convert a trust into  
3 a unitrust, the court shall require the trustee either to convert into a unitrust or to  
4 reconvert from a unitrust;

5 (4) to the extent that the court is unable, after applying (1) - (3) of this  
6 subsection, to restore the beneficiaries, the trust, or both to the positions they would  
7 have occupied if the fiduciary had not abused the fiduciary's discretion, the court may  
8 require the fiduciary to pay an appropriate amount from the fiduciary's own funds to  
9 one or more of the beneficiaries, the trust, or both.

## 10 Article 2. Conversion to Unitrust.

11 Sec. 13.38.300. Power to convert to unitrust. Unless expressly prohibited  
12 by the governing instrument, a trustee may release the power to adjust under  
13 AS 13.38.210 and may convert a trust into a unitrust as described in AS 13.38.300 -  
14 13.38.410 if

15 (1) the trustee determines that the conversion will enable the trustee to  
16 better carry out the intent of the settlor or testator and the purposes of the trust;

17 (2) the trustee gives written notice of the trustee's intention to release  
18 the power to adjust, of the trustee's intention to convert the trust into a unitrust, and of  
19 how the unitrust will operate, including what initial decisions the trustee will make  
20 under this section, to all the sui juris beneficiaries who

21 (A) are currently eligible to receive income from the trust;

22 (B) would be eligible, if a power of appointment were not  
23 exercised, to receive income from the trust if the interest of all of the  
24 beneficiaries eligible to receive income under (A) of this paragraph were to  
25 terminate immediately before the giving of the notice; and

26 (C) would, if a power of appointment were not exercised,  
27 receive a distribution of principal if the trust were to terminate immediately  
28 before the giving of the notice;

29 (3) there are at least one sui juris beneficiary under (2)(A) of this  
30 section and at least one sui juris beneficiary under (2)(B) or (C) of this section; and

31 (4) a sui juris beneficiary does not object to the conversion to a unitrust

1 in a writing delivered to the trustee within 60 days after the mailing of the notice under  
2 (2) of this section.

3 **Sec. 13.38.310. Judicially approved conversion.** (a) A trustee may petition  
4 the court to approve the conversion to a unitrust if

5 (1) a beneficiary timely objects to the conversion to a unitrust; or

6 (2) there is not a sui juris beneficiary who is eligible under  
7 AS 13.38.300(2)(A), and there is not a sui juris beneficiary who is eligible under  
8 AS 13.38.300(2)(B) or (C).

9 (b) A beneficiary may request a trustee to convert to a unitrust. If the trustee  
10 does not convert, the beneficiary may petition the superior court to order the  
11 conversion.

12 (c) The superior court shall approve the conversion or direct the requested  
13 conversion if the court concludes that the conversion will enable the trustee to better  
14 carry out the intent of the settlor or testator and the purposes of the trust.

15 **Sec. 13.38.320. Factors to be considered.** In deciding whether to exercise  
16 the power conferred by AS 13.38.300, a trustee may consider, among other things,

17 (1) the size of the trust;

18 (2) the nature and estimated duration of the trust;

19 (3) the liquidity and distribution requirements of the trust;

20 (4) the need for regular distributions and preservation and appreciation  
21 of capital;

22 (5) the expected tax consequences of the conversion;

23 (6) the assets held in the trust; the extent to which they consist of  
24 financial assets, interests in closely held enterprises, tangible and intangible personal  
25 property, or real property; and the extent to which an asset is used by a beneficiary;

26 (7) to the extent reasonably known to the trustee, the need of the  
27 beneficiaries for present and future distributions authorized or required by the  
28 governing instrument;

29 (8) whether and to what extent the governing instrument gives the  
30 trustee the power to invade principal or accumulate income or prohibits the trustee  
31 from invading principal or accumulating income and the extent to which the trustee

1 has exercised a power from time to time to invade principal or accumulate income;

2 (9) the actual and anticipated effect of economic conditions on  
3 principal and income and the effects of inflation and deflation.

4 **Sec. 13.38.330. Directions after conversion.** (a) After a trust is converted to  
5 a unitrust, the trustee shall

6 (1) follow an investment policy seeking a total return for the  
7 investments held by the trust, whether the return is to be derived from

8 (A) appreciation of capital;

9 (B) earnings and distributions from capital; or

10 (C) both (A) and (B) of this paragraph; and

11 (2) make regular distributions in accordance with the governing  
12 instrument construed in accordance with the provisions of this section.

13 (b) After a trust has been converted to a unitrust, "income" in the governing  
14 instrument means an annual distribution equal to four percent of the net fair market  
15 value, as determined annually, of the trust's assets, whether the assets would be  
16 considered income or principal under other provisions of this chapter.

17 (c) After a trust has been administered as a unitrust for three years, the four  
18 percent amount referred to in (b) of this section shall be averaged over the three  
19 preceding years of the trust.

20 **Sec. 13.38.340. Discretion of trustee regarding conversion.** The trustee  
21 may in the trustee's discretion, from time to time, determine

22 (1) the effective date of a conversion to a unitrust;

23 (2) the provisions for prorating a unitrust distribution for a short year  
24 in which a beneficiary's right to payments commences or ceases;

25 (3) the frequency of unitrust distributions during the year;

26 (4) the effect of other payments from or contributions to the trust on  
27 the trust's valuation;

28 (5) whether to value the trust's assets annually or more frequently;

29 (6) what valuation dates to use;

30 (7) how frequently to value nonliquid assets and whether to estimate  
31 their value;

1 (8) whether to omit trust property occupied or possessed by a  
2 beneficiary from the calculations; and

3 (9) other matters necessary for the proper functioning of the unitrust.

4 **Sec. 13.38.350. Unitrust deductions and distributions.** (a) Expenses that  
5 would be deducted from income if the trust were not a unitrust may not be deducted  
6 from the unitrust distribution.

7 (b) Unless otherwise provided by the governing instrument, a unitrust  
8 distribution shall be considered to have been paid from net income as net income  
9 would be determined if the trust were not a unitrust. To the extent net income is  
10 insufficient, the unitrust distribution shall be considered to have been paid from net  
11 realized short-term capital gains. To the extent income and net realized short-term  
12 capital gains are insufficient, the unitrust distribution shall be considered to have been  
13 paid from net realized long-term capital gains. To the extent income and net realized  
14 short-term and long-term capital gains are insufficient, the unitrust distribution shall  
15 be paid from the principal of the trust.

16 **Sec. 13.38.360. Court orders regarding unitrust.** The trustee or, if the  
17 trustee declines to petition the court, a beneficiary may petition the court to

18 (1) select a payout percentage different than four percent;

19 (2) provide for a distribution of net income, as would be determined if  
20 the trust were not a unitrust, in excess of the unitrust distribution if the distribution is  
21 necessary to preserve a tax benefit;

22 (3) average the valuation of the trust's net assets over a period other  
23 than three years.

24 **Sec. 13.38.370. Effects of conversion.** A conversion to a unitrust does not  
25 affect a provision in the governing instrument directing or authorizing the trustee to  
26 distribute principal or authorizing a beneficiary to withdraw a portion or all of the  
27 principal.

28 **Sec. 13.38.380. Prohibited conversions; exception.** (a) A trustee may not  
29 convert a trust into a unitrust if

30 (1) payment of the unitrust distribution would change the amount  
31 payable to a beneficiary as a fixed annuity or a fixed fraction of the value of the trust

1 assets;

2 (2) the unitrust distribution would be made from an amount that is  
3 permanently set aside for charitable purposes under the governing instrument and for  
4 which a federal estate or gift tax deduction has been taken;

5 (3) possessing or exercising the power to convert would cause an  
6 individual to be treated as the owner of all or part of the trust for federal income tax  
7 purposes, and the individual would not be treated as the owner if the trustee did not  
8 possess the power to convert;

9 (4) possessing or exercising the power to convert would cause all or  
10 part of the trust assets to be subject to federal estate or gift tax with respect to an  
11 individual, and the assets would not be subject to federal estate or gift tax with respect  
12 to the individual if the trustee did not possess the power to convert;

13 (5) the conversion would result in the disallowance of a federal estate  
14 tax or gift tax marital deduction that would be allowed if the trustee did not have the  
15 power to convert; or

16 (6) the trustee is a beneficiary of the trust.

17 (b) Notwithstanding (a)(2) of this section, a trustee may elect to convert a trust  
18 to a unitrust if both the income and principal of the trust being converted to a unitrust  
19 are permanently set aside for charitable purposes and if the provisions of  
20 AS 13.38.440 - 13.38.490 are followed.

21 **Sec. 13.38.390. Permissible conversion where otherwise prohibited.** (a) If  
22 AS 13.38.380(a)(3), (4), or (6) applies to a trustee and there is more than one trustee, a  
23 co-trustee to whom the provision does not apply may convert the trust, unless the  
24 exercise of the power by the remaining trustee is prohibited by the governing  
25 instrument.

26 (b) If AS 13.38.380(a)(3), (4), or (6) applies to all the trustees, the trustees  
27 may petition the court to direct a conversion.

28 **Sec. 13.38.400. Reconversion from a unitrust.** A trustee may reconvert a  
29 trust that has been converted into a unitrust under AS 13.38.300 by following the same  
30 procedures provided in AS 13.38.300 - 13.38.410 for converting a trust into a unitrust.  
31 If a unitrust is reconverted under this section, the trustee's power to adjust under

1 AS 13.38.210 applies to the trustee after the reconversion.

2 **Sec. 13.38.410. Release of power to convert to unitrust.** (a) A trustee may  
3 release the power conferred by AS 13.38.300 to convert to a unitrust if the trustee

4 (1) is uncertain about whether possessing or exercising the power will  
5 cause a result described in AS 13.38.380(a)(3), (4), or (5); or

6 (2) determines that possessing or exercising the power will or may  
7 deprive the trust of a tax benefit or impose a tax burden not described in  
8 AS 13.38.380.

9 (b) The release of a power under (a) of this section may be permanent or for a  
10 specified period, including a period measured by the life of an individual.

### 11 **Article 3. Charitable Trust Election.**

12 **Sec. 13.38.440. Charitable trust election.** The trustee of a trust held  
13 exclusively for charitable purposes may elect to be governed by AS 13.38.440 -  
14 13.38.490 unless the governing instrument expressly provides that the election  
15 provided by AS 13.38.440 - 13.38.490 is not available.

16 **Sec. 13.38.450. Eligibility for charitable trust election.** To make an election  
17 under AS 13.38.440 - 13.38.490, the trustee shall adopt and follow an investment  
18 policy seeking a total return for the investments held by the trust, whether the return is  
19 to be derived from appreciation of capital or earnings and distributions with respect to  
20 capital or both. The policy constituting the election must be in writing, must be  
21 maintained as part of the permanent records of the trust, and must recite that it  
22 constitutes an election to be governed by AS 13.38.440 - 13.38.490.

23 **Sec. 13.38.460. Selection of percentage after charitable trust election.** (a)  
24 After a trustee has elected under AS 13.38.440 for the trust to be governed by  
25 AS 13.38.440 - 13.38.490, the trustee shall, in a writing maintained as part of the  
26 permanent records of the trust, select the percentage of the value of the trust that will  
27 be considered income and determine that it is consistent with the long-term  
28 preservation of the real value of the principal of the trust, but the percentage may not  
29 be less than two percent or more than seven percent each year of the principal value of  
30 the trust. The trustee may elect to change a percentage previously selected if the  
31 trustee determines that the new percentage is consistent with the long-term

1 preservation of the real value of the principal of the trust, but may not change the  
2 percentage more frequently than once every 10 years.

3 (b) For a charitable trust required by 26 U.S.C. 4942 (Internal Revenue Code)  
4 to distribute a higher amount than the percentage selected under (a) of this section, the  
5 amount required by 26 U.S.C. 4942 (Internal Revenue Code) controls over the  
6 percentage selected.

7 **Sec. 13.38.470. Revocation of charitable trust election.** The trustee may  
8 revoke an election to be governed by AS 13.38.440 - 13.38.490 if the revocation is  
9 made as part of an alternative investment policy seeking the long-term preservation of  
10 the real value of the principal of the trust. The revocation and alternative investment  
11 policy must be in writing and maintained as part of the permanent records of the trust.

12 **Sec. 13.38.480. Value determination.** For the purposes of applying  
13 AS 13.38.440 - 13.38.490, the value of the trust is the fair market value of the cash  
14 and other assets held by the trustee with respect to the trust, whether these assets  
15 would be considered income or principal under the other provisions of this chapter,  
16 determined at least annually. In the discretion of the trustee, the value of the trust may  
17 be averaged over a period of three or more preceding years when the trust has been  
18 administered as a unitrust under this section for at least three years.

19 **Sec. 13.38.490. Definitions.** In AS 13.38.440 - 13.38.490, except as  
20 otherwise expressly stated in AS 13.38.440 - 13.38.490,

21 (1) "income" means the percentage of the value of the trust computed  
22 under AS 13.38.440 - 13.38.490;

23 (2) "principal" means all assets other than those identified as income in  
24 (1) of this section that are held by the trustee with respect to the trust.

25 **Article 4. Decedent's Estate or Terminating Income Interest.**

26 **Sec. 13.38.500. Determination and distribution of net income.** After a  
27 decedent dies in the case of an estate, or after an income interest in a trust ends, a  
28 fiduciary

29 (1) of an estate or of a terminating income interest shall determine the  
30 amount of net income and net principal receipts received from property specifically  
31 given to a beneficiary under (5) of this section and the provisions applicable to trustees

1 in AS 13.38.550 - 13.38.860; the fiduciary shall distribute the net income and net  
2 principal receipts to the beneficiary who is to receive the specific property;

3 (2) shall distribute to a beneficiary who receives a pecuniary amount  
4 outright and shall allocate to a pecuniary amount in trust the interest, other income, or  
5 other amount provided by the governing instrument from net income determined under  
6 (3) of this section or from principal to the extent that net income is insufficient;

7 (3) shall determine the remaining net income of a decedent's estate or a  
8 terminating income interest under the provisions applicable to trustees in  
9 AS 13.38.550 - 13.38.860 and by

10 (A) including in net income all income from property used to  
11 discharge liabilities; and

12 (B) paying from principal the debts, the funeral expenses, the  
13 costs of disposition of remains, the family allowance under AS 13.12.404, fees  
14 of personal representatives and their attorneys and accountants, and the taxes,  
15 related interest, and penalties described in AS 13.38.810(a)(7) that are  
16 apportioned to the estate or terminating income interest by the governing  
17 instrument or applicable law;

18 (4) shall distribute the net income remaining after distributions  
19 required by (2) of this section in the manner described in AS 13.38.510 to all other  
20 beneficiaries;

21 (5) may not reduce principal or income receipts from property  
22 described in (1) of this section because of a payment described in AS 13.38.700 or  
23 13.38.710 to the extent that the governing instrument or applicable law requires the  
24 fiduciary to make the payment from assets other than the property or to the extent that  
25 the fiduciary recovers or expects to recover the payment from a third party; the net  
26 income and principal receipts from the property are determined by

27 (A) including all of the amounts the fiduciary receives or pays  
28 with respect to the property, whether those amounts accrued or became due  
29 before, on, or after the date of a decedent's death or an income interest's  
30 terminating event; and

31 (B) making a reasonable provision for amounts that the

1 fiduciary believes the estate or terminating income interest may become  
2 obligated to pay after the property is distributed.

3 **Sec. 13.38.510. Distribution to residuary and remainder beneficiaries.** (a)

4 Each beneficiary described in AS 13.38.500(4) is entitled to receive a portion of the  
5 net income equal to the beneficiary's fractional interest in undistributed principal  
6 assets, using values as of the distribution date. If a fiduciary makes more than one  
7 distribution of assets to beneficiaries to whom this section applies, each beneficiary,  
8 including one who does not receive part of the distribution, is entitled, as of each  
9 distribution date, to the net income the fiduciary has received after the date of death or  
10 terminating event or earlier distribution date but has not distributed as of the current  
11 distribution date.

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

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

18 (2) the beneficiary's fractional interest in the undistributed principal  
19 assets shall be calculated without regard to property specifically given to a beneficiary  
20 and property required to pay pecuniary amounts;

21 (3) the beneficiary's fractional interest in the undistributed principal  
22 assets shall be calculated on the basis of the aggregate value of those assets as of the  
23 distribution date without reducing the value by any unpaid principal obligation.

24 (c) If a fiduciary does not distribute all of the collected but undistributed net  
25 income to each person as of a distribution date, the fiduciary shall maintain  
26 appropriate records showing the interest of each beneficiary in that net income.

27 (d) To the extent that the fiduciary considers it appropriate, if this section  
28 applies to the income from an asset, the fiduciary may apply the rules in this section to  
29 net gain or loss from the disposition of a principal asset realized after the date of death  
30 or terminating event or an earlier distribution date.

31 (e) For the purposes of this section, the distribution date may be the date as of

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

3 **Article 5. Apportionment at Beginning and End of Income Interest.**

4 **Sec. 13.38.550. When right to income begins and ends.** (a) An income  
5 beneficiary is entitled to net income from the date on which the income interest  
6 begins. An income interest begins

7 (1) on the date specified in the governing instrument; or

8 (2) if a date is not specified, on the date an asset becomes subject to a  
9 trust or successive income interest.

10 (b) An asset becomes subject to a trust

11 (1) on the date it is transferred to the trust, in the case of an asset that is  
12 transferred to a trust during the transferor's life;

13 (2) on the date of a testator's death, in the case of an asset that becomes  
14 subject to a trust by reason of a will, even if there is an intervening period of  
15 administration of the testator's estate; or

16 (3) on the date of an individual's death, in the case of an asset that is  
17 transferred to a fiduciary by a third party because of the individual's death.

18 (c) An asset becomes subject to a successive income interest on the day after  
19 the preceding income interest ends, as determined under (d) of this section, even if  
20 there is an intervening period of administration to wind up the preceding income  
21 interest.

22 (d) An income interest ends on

23 (1) the day before an income beneficiary dies or another terminating  
24 event occurs; or

25 (2) the last day of a period during which there is not a beneficiary to  
26 whom a trustee may distribute income.

27 **Sec. 13.38.560. Apportionment of receipts and disbursements when**  
28 **decedent dies or income interest begins.** (a) Unless AS 13.38.500(1) applies, a  
29 trustee shall allocate an income receipt or disbursement to principal if its due date  
30 occurs before

31 (1) a decedent dies, in the case of an estate; or

1 (2) an income interest begins, in the case of a trust or successive  
2 income interest.

3 (b) A trustee shall allocate an income receipt or disbursement to income if its  
4 due date occurs on or after the date on which a decedent dies or an income interest  
5 begins and its due date is periodic. An income receipt or disbursement shall be treated  
6 as accruing from day to day if its due date is not periodic or it does not have a due  
7 date. The portion of the receipt or disbursement accruing before the date on which a  
8 decedent dies or an income interest begins shall be allocated to principal, and the  
9 balance shall be allocated to income.

10 (c) An item of income or an obligation is due on the date the payer is required  
11 to make a payment. If a payment date is not stated, there is not a due date for the  
12 purposes of this chapter. Distributions to shareholders or other owners from an entity  
13 to which AS 13.38.600 applies are considered to be due on the date fixed by the entity  
14 for determining who is entitled to receive the distribution or, if a date is not fixed, on  
15 the declaration date for the distribution. A due date is periodic for receipts or  
16 disbursements that must be paid at regular intervals under a lease or an obligation to  
17 pay interest or if an entity customarily makes distributions at regular intervals.

18 **Sec. 13.38.570. Apportionment when income interest ends.** (a) When a  
19 mandatory income interest ends, the trustee shall pay to a mandatory income  
20 beneficiary who survives that date, or the estate of a deceased mandatory income  
21 beneficiary whose death causes the interest to end, the beneficiary's share of the  
22 undistributed income that is not disposed of under the governing instrument unless the  
23 beneficiary has an unqualified power to revoke more than five percent of the trust  
24 immediately before the income interest ends. In the case of the beneficiary who has an  
25 unqualified power to revoke more than five percent of the trust immediately before the  
26 income interest ends, the undistributed income from the portion of the trust that may  
27 be revoked shall be added to principal.

28 (b) When a trustee's obligation to pay a fixed annuity or a fixed fraction of the  
29 value of the trust's assets ends, the trustee shall prorate the final payment if and to the  
30 extent required by applicable law to accomplish a purpose of the trust or its settlor or  
31 testator relating to income, gift, estate, or other tax requirements.

1 (c) In this section, "undistributed income" means net income received before  
2 the date on which an income interest ends, but does not include an item of income or  
3 expense that is due or accrued or net income that has been added or is required to be  
4 added to principal under the governing instrument.

5 **Article 6. Allocation of Receipts during Administration of Trust.**

6 **Sec. 13.38.600. Character of receipts.** (a) Except as otherwise provided in  
7 this section, a trustee shall allocate to income money received from an entity,  
8 including reinvested cash dividends.

9 (b) A trustee shall allocate the following receipts from an entity to principal:

- 10 (1) property other than money excluding reinvested cash dividends;  
11 (2) money received in one distribution or a series of related  
12 distributions in exchange for part or all of a trust's interest in the entity;  
13 (3) money received in total or partial liquidation of the entity;  
14 (4) money received from an entity that is a regulated investment  
15 company or a real estate investment trust if the money distributed is a short-term or  
16 long-term capital gain dividend for federal income tax purposes.

17 (c) Money is received in partial liquidation

- 18 (1) to the extent that the entity, at or near the time of a distribution,  
19 indicates that it is a distribution in partial liquidation; or  
20 (2) if the total amount of money and property received in a distribution  
21 or series of related distributions is greater than 20 percent of the entity's gross assets,  
22 as shown by the entity's year-end financial statements immediately preceding the  
23 initial receipt.

24 (d) Money is not received in partial liquidation, and it may not be taken into  
25 account under (c)(2) of this section, to the extent that it does not exceed the amount of  
26 income tax that a trustee or beneficiary must pay on taxable income of the entity that  
27 distributes the money.

28 (e) A trustee may rely upon a statement made by an entity about the source or  
29 character of a distribution if the statement is made at or near the time of distribution by  
30 the entity's board of directors or other person or group of persons authorized to  
31 exercise powers to pay money or transfer property comparable to those of a

1 corporation's board of directors.

2 (f) In this section, "entity" means a corporation, partnership, limited liability  
3 company, regulated investment company, real estate investment trust, common trust  
4 fund, or another organization in which a trustee has an interest, but does not include

5 (1) a trust or estate to which AS 13.38.610 applies;

6 (2) a business or activity to which AS 13.38.620 applies;

7 (3) a payment to which AS 13.38.680 applies; or

8 (4) an asset-backed security to which AS 13.38.740 applies.

9 **Sec. 13.38.610. Distribution from trust or estate.** (a) A trustee shall  
10 allocate to income an amount received as a distribution of income from a trust or an  
11 estate in which the trust has an interest other than a purchased interest.

12 (b) A trustee shall allocate to principal an amount received as a distribution of  
13 principal from a trust or estate in which the trust has an interest other than a purchased  
14 interest.

15 (c) If a trustee purchases an interest in a trust that is an investment entity, or a  
16 decedent or donor transfers an interest in a trust that is an investment entity to a  
17 trustee, AS 13.38.600 or 13.38.740 applies to a receipt from the trust.

18 **Sec. 13.38.620. Business and other activities conducted by trustee.** (a) If a  
19 trustee that conducts a business or other activity determines that it is in the best  
20 interest of all the beneficiaries to account separately for the business or other activity  
21 instead of accounting for it as part of the trust's general accounting records, the trustee  
22 may maintain separate accounting records for the transactions of the business or other  
23 activity, whether or not the assets of the business or other activity are segregated from  
24 other trust assets.

25 (b) A trustee who accounts separately for a business or other activity may  
26 determine the extent to which

27 (1) its net cash receipts are retained for working capital, the acquisition  
28 or replacement of fixed assets, and other reasonably foreseeable needs of the business  
29 or activity; and

30 (2) the remaining net cash receipts are accounted for as principal or  
31 income in the trust's general accounting records.

1 (c) If a trustee sells assets of the business or other activity, other than in the  
2 ordinary course of the business or activity, the trustee shall account for the net amount  
3 received as principal in the trust's general accounting records to the extent the trustee  
4 determines that the amount received is not required any longer in the conduct of the  
5 business.

6 (d) Activities for which a trustee may maintain separate accounting records  
7 include

8 (1) retail, manufacturing, service, and other traditional business  
9 activities;

10 (2) farming;

11 (3) raising and selling livestock and other animals;

12 (4) management of rental properties;

13 (5) extraction of minerals and other natural resources;

14 (6) timber operations; and

15 (7) activities to which AS 13.38.730 applies.

16 **Sec. 13.38.630. Principal receipts.** A trustee shall allocate to principal any of  
17 the following:

18 (1) to the extent not allocated to income under this chapter, assets  
19 received from

20 (A) a transferor during the transferor's lifetime;

21 (B) a decedent's estate;

22 (C) a trust with a terminating income interest; or

23 (D) a payor under a contract naming the trust or its trustee as  
24 beneficiary;

25 (2) money or other property received from a principal asset's sale,  
26 exchange, liquidation, or change in form, including realized profit subject to  
27 AS 13.38.600 -13.38.740;

28 (3) amounts recovered from third parties to reimburse the trust because  
29 of disbursements described in AS 13.38.810(a)(8) or for other reasons, to the extent  
30 not based on the loss of income, except that a separate award made for the loss of  
31 income with respect to an accounting period during which a current income

1 beneficiary had a mandatory income interest is income;

2 (4) net income received in an accounting period during which there is  
3 not a beneficiary to whom a trustee may or must distribute income;

4 (5) other receipts as provided in AS 13.38.670 - 13.38.740.

5 **Sec. 13.38.640. Rental property.** (a) To the extent that a trustee accounts for  
6 receipts from rental property under this section, the trustee shall allocate an amount  
7 received as rent of real or personal property to income, including an amount received  
8 for cancellation or renewal of a lease.

9 (b) An amount received as a refundable deposit, including a security deposit  
10 or a deposit that is to be applied as rent for future periods,

11 (1) shall be added to principal;

12 (2) shall be held subject to the terms of the lease; and

13 (3) is not available for distribution to a beneficiary until the trustee's  
14 contractual obligations have been satisfied with respect to that amount.

15 **Sec. 13.38.650. Obligation to pay money.** (a) An amount received as  
16 interest, whether determined at a fixed, variable, or floating rate, on an obligation to  
17 pay money to the trustee, including an amount received as consideration for prepaying  
18 principal, shall be allocated to income without any provision for amortization of  
19 premium.

20 (b) A trustee shall allocate to principal an amount received from the sale,  
21 redemption, or other disposition of an obligation to pay money to the trustee more than  
22 one year after it is purchased or acquired by the trustee, including an obligation if the  
23 purchase price or value of the obligation when it is acquired is less than its value at  
24 maturity. If the obligation matures within one year after it is purchased or acquired by  
25 the trustee, an amount received in excess of its purchase price or its value when  
26 acquired by the trust shall be allocated to income.

27 (c) This section does not apply to an obligation to which AS 13.38.680,  
28 13.38.690, 13.38.700, 13.38.710, 13.38.720, 13.38.730, or 13.38.740 applies.

29 **Sec. 13.38.660. Insurance policies and similar contracts.** (a) Except as  
30 otherwise provided in (b) or (c) of this section, a trustee shall allocate to principal the  
31 proceeds of a life insurance policy or other contract in which the trust or its trustee is

1 named as beneficiary, including a contract that insures the trust or its trustee against  
2 loss for damage to, destruction of, or loss of title to a trust asset. If the premiums on  
3 the policy or contract are paid from income, the trustee shall allocate dividends on the  
4 policy or contract to income. If the premiums on the policy or contract are paid from  
5 principal, the trustee shall allocate dividends on the policy or contract to principal.

6 (b) Except as provided in (c) of this section, a trustee shall allocate to income  
7 proceeds of a contract that insures the trustee against

8 (1) loss of occupancy or other use by an income beneficiary;

9 (2) loss of income; or

10 (3) subject to AS 13.38.620, loss of profits from a business.

11 (c) This section does not apply to a contract to which AS 13.38.680 applies.

12 **Sec. 13.38.670. Insubstantial allocations not required.** If a trustee  
13 determines that an allocation between principal and income required by AS 13.38.680,  
14 13.38.690, 13.38.700, 13.38.710, or 13.38.740 is insubstantial, the trustee may allocate  
15 the entire amount to principal unless one of the circumstances described in  
16 AS 13.38.210(c) applies to the allocation. This power may be exercised by a co-  
17 trustee in the circumstances described in AS 13.38.210(d) and may be released for the  
18 reasons and in the manner described in AS 13.38.210(e). An allocation is presumed to  
19 be insubstantial if

20 (1) the amount of the allocation would increase or decrease net income  
21 in an accounting period, as determined before the allocation, by less than five percent;  
22 or

23 (2) the value of the asset producing the receipt for which the allocation  
24 would be made is less than five percent of the total value of the trust's assets at the  
25 beginning of the accounting period.

26 **Sec. 13.38.680. Retirement benefits, individual retirement accounts,**  
27 **deferred compensation, annuities, and similar payments.** (a) The trustee shall  
28 allocate to income the greater of the portion of a payment characterized by the payor  
29 as interest or a dividend, as a remittance in place of interest or a dividend, or as  
30 imputed interest for federal income tax purposes. The balance of the payment shall be  
31 allocated to principal.

1 (b) If a part of a payment under a contract calling for equal installments over a  
2 fixed period of time is not allocable to income under the provisions of (a) of this  
3 section, the difference between the trust's acquisition value of the contract and the total  
4 expected return shall be considered to be interest. The trustee shall allocate to income  
5 the portion of each payment equivalent to interest on the then unpaid principal balance  
6 at the rate specified in the contract or at a rate necessary to amortize the difference  
7 between the expected return and the acquisition value, where that rate is readily  
8 ascertainable by the trustee.

9 (c) If there is not a portion of a payment from a separate fund held exclusively  
10 for the benefit of the trust that is allocable to income under (a) or (b) of this section,  
11 but the internal net income of the fund determined as if the fund were a separate trust  
12 subject to AS 13.38.500 -13.38.860 is readily ascertainable by the trustee, the portion  
13 of the payment equal to the then undistributed net income of the fund realized since  
14 the trust acquired its interest in the fund is considered to be a distribution of income  
15 and shall be allocated to the trust income account. The balance of the payment  
16 described in this subsection shall be allocated to principal.

17 (d) A trustee shall allocate 10 percent of the part of the payment that is  
18 required to be made during the accounting period to income and the balance to  
19 principal if there is not a part of the payment that is allocable to income under (a) - (c)  
20 of this section and all or part of the payment is required to be made. The trustee shall  
21 allocate the entire payment to principal if a part of a payment is not required to be  
22 made or the payment received is the entire amount to which the trustee is entitled. In  
23 this subsection, a payment is not "required to be made" to the extent that it is made  
24 because the trustee exercises a right of withdrawal.

25 (e) If, to obtain a federal estate or gift tax marital deduction for a trust, the  
26 trustee must allocate more of a payment to income than provided for by this section,  
27 the trustee shall allocate the additional amount necessary to obtain the marital  
28 deduction to income.

29 (f) This section does not apply to payments to which AS 13.38.690 applies.

30 (g) In this section, "payment" means a payment that a trustee may receive over  
31 a fixed period of time or during the life of one or more individuals because of services

1 rendered or property transferred to the payor in exchange for future payments, and  
2 includes

3 (1) a payment made in money or property from the payor's general  
4 assets or from a separate fund created by the payor or another person;

5 (2) a payment on or from

6 (A) an installment contract or note;

7 (B) a private or commercial annuity;

8 (C) a deferred compensation agreement;

9 (D) an employee death benefit;

10 (E) an individual retirement account; or

11 (F) a pension plan, profit-sharing plan, stock plan, bonus plan,  
12 or stock-ownership plan.

13 **Sec. 13.38.690. Liquidating asset.** (a) A trustee shall allocate 10 percent of  
14 the receipts from a liquidating asset to income and the balance to principal.

15 (b) In this section, "liquidating asset"

16 (1) means

17 (A) an asset the value of which will diminish or terminate  
18 because the asset is expected to produce receipts for a period of limited  
19 duration; or

20 (B) a leasehold, patent, copyright, royalty right, and right to  
21 receive payments during a period of more than one year under an arrangement  
22 that does not provide for the payment of interest on the unpaid balance;

23 (2) does not include

24 (A) a payment subject to AS 13.38.680;

25 (B) resources subject to AS 13.38.700;

26 (C) timber subject to AS 13.38.710;

27 (D) an activity subject to AS 13.38.730;

28 (E) an asset subject to AS 13.38.740; or

29 (F) an asset for which the trustee establishes a reserve for  
30 depreciation under AS 13.38.830.

31 **Sec. 13.38.700. Minerals, water, and other natural resources.** (a) To the

1 extent that a trustee accounts for receipts from an interest in minerals or other natural  
2 resources under this section, the trustee shall allocate them as follows:

3 (1) if received as nominal delay rent or nominal annual rent on a lease,  
4 a receipt shall be allocated to income;

5 (2) if received from a production payment, a receipt shall be allocated  
6 to income if and to the extent that the agreement creating the production payment  
7 provides a factor for interest or its equivalent; the balance shall be allocated to  
8 principal;

9 (3) if an amount received as a royalty, shut-in-well payment, take-or-  
10 pay payment, bonus, or delay rental is more than nominal, 66 2/3 percent shall be  
11 allocated to principal, and the balance shall be allocated to income;

12 (4) if an amount is received from a working interest or any other  
13 interest not provided for in (1) - (3) of this subsection, 66 2/3 percent of the net  
14 amount received shall be allocated to principal, and the balance shall be allocated to  
15 income.

16 (b) An amount received on account of an interest in renewable water shall be  
17 allocated to income. An amount received on account of an interest in nonrenewable  
18 water shall be allocated as follows:

19 (1) 66 2/3 percent of the amount shall be allocated to principal; and

20 (2) the balance shall be allocated to income.

21 (c) This chapter applies whether or not a decedent or donor was extracting  
22 minerals, water, or other natural resources before the interest became subject to the  
23 trust.

24 **Sec. 13.38.710. Timber.** (a) To the extent that a trustee accounts for receipts  
25 from the sale of timber and related products under this section, the trustee shall  
26 allocate the net receipts

27 (1) to income, to the extent that the amount of timber removed from  
28 the land does not exceed the rate of growth of the timber during the accounting periods  
29 in which a beneficiary has a mandatory income interest;

30 (2) to principal, to the extent that the amount of timber removed from  
31 the land exceeds the rate of growth of the timber, or the net receipts are from the sale

1 of standing timber;

2 (3) between income and principal, by determining the amount of  
3 timber removed from the land under the lease or contract and applying the rules in (1)  
4 and (2) of this subsection if the net receipts are from the lease of timberland or a  
5 contract to cut timber from land owned by a trust;

6 (4) to principal to the extent that advance payments, bonuses, and other  
7 payments are not allocated under (1) - (3) of this subsection.

8 (b) In determining net receipts to be allocated under (a) of this section, a  
9 trustee shall deduct and transfer to principal a reasonable amount for depletion.

10 (c) This chapter applies whether or not a decedent or transferor was harvesting  
11 timber from the property before it became subject to the trust.

12 **Sec. 13.38.720. Property not productive of income.** (a) If a federal estate or  
13 gift tax marital deduction is allowed for all or part of a trust whose income is required  
14 to be paid to the settlor's or testator's spouse and whose assets consist substantially of  
15 property that does not provide the spouse with sufficient income from or use of the  
16 trust assets, and if the amounts that the trustee transfers from principal to income  
17 under AS 13.38.210 and that the trustee distributes to the spouse from principal under  
18 the governing instrument are insufficient to provide the spouse with the beneficial  
19 enjoyment required to obtain the marital deduction, the spouse may require the trustee  
20 to make property productive of income, convert property within a reasonable time, or  
21 exercise the power conferred by AS 13.38.210(a). The trustee may decide which  
22 action or combination of actions to take.

23 (b) In cases not governed by (a) of this section, proceeds from the sale or other  
24 disposition of an asset are principal without regard to the amount of income the asset  
25 produces during any accounting period.

26 **Sec. 13.38.730. Derivatives and options.** (a) To the extent that a trustee  
27 does not account under AS 13.38.620 for transactions in derivatives, the trustee shall  
28 allocate receipts from and disbursements made in connection with those transactions  
29 to principal.

30 (b) If a trustee grants an option to buy property from the trust, whether or not  
31 the trust owns the property when the option is granted, grants an option that permits

1 another person to sell property to the trust, or acquires an option to buy property for  
2 the trust or an option to sell an asset owned by the trust, and the trustee or other owner  
3 of the asset is required to deliver the asset if the option is exercised, an amount  
4 received for granting the option shall be allocated to principal. An amount paid to  
5 acquire the option shall be paid from principal. A gain or loss realized upon the  
6 exercise of an option, including an option granted to a settlor or testator of the trust for  
7 services rendered, shall be allocated to principal.

8 (c) In this section, "derivative" means a contract or financial instrument or a  
9 combination of contracts and financial instruments that gives a trust the right or  
10 obligation to participate in some or all changes in the price of a tangible or intangible  
11 asset or group of assets, or changes in a rate, an index of prices or rates, or another  
12 market indicator for an asset or a group of assets.

13 **Sec. 13.38.740. Asset-backed securities.** (a) If a trust receives a payment  
14 from interest or other current return and from other proceeds of the collateral financial  
15 assets, the trustee shall allocate the portion of the payment that the payor identifies as  
16 being from interest or other current return to income, and the trustee shall allocate the  
17 balance of the payment to principal.

18 (b) If a trust receives one or more payments in exchange for the trust's entire  
19 interest in an asset-backed security in one accounting period, the trustee shall allocate  
20 the payments to principal. If a payment is one of a series of payments that will result  
21 in the liquidation of the trust's interest in the security over more than one accounting  
22 period, the trustee shall allocate 10 percent of the payment to income and the balance  
23 to principal.

24 (c) In this section, "asset-backed security"

25 (1) means an asset whose value is based on the right it gives the owner  
26 to receive distributions from the proceeds of financial assets that provide collateral for  
27 the security;

28 (2) includes an asset that gives the owner the right to receive from the  
29 collateral financial assets only the interest or other current return or only the proceeds  
30 other than interest or current return;

31 (3) does not include an asset to which AS 13.38.600 or 13.38.680

1 applies.

2 **Article 7. Allocation of Disbursements During Administration of Trust.**

3 **Sec. 13.38.800. Mandatory disbursements from income.** A trustee shall  
4 make the following disbursements from income:

- 5 (1) interest, except interest on taxes described in AS 13.38.810(a)(7);  
6 (2) ordinary repairs;  
7 (3) real estate and other regularly recurring taxes assessed against  
8 principal;  
9 (4) recurring premiums on fire or other insurance covering the loss of a  
10 principal asset or the loss of income from or use of the asset.

11 **Sec. 13.38.810. Mandatory disbursements from principal.** (a) A trustee  
12 shall make the following disbursements from principal:

- 13 (1) extraordinary expenses incurred in connection with the  
14 administration, management, or preservation of trust property and the distribution of  
15 income;  
16 (2) extraordinary repairs;  
17 (3) compensation for legal services to the trustee;  
18 (4) expenses in connection with accountings and judicial or other  
19 proceedings, including proceedings to construe, modify, or reform the trust or to  
20 protect the trust or its property;  
21 (5) payments on the principal of a trust debt;  
22 (6) premiums paid on a policy of insurance not described in  
23 AS 13.38.800(4) if the trust is the owner and beneficiary;  
24 (7) estate, inheritance, and other transfer taxes, including interest and  
25 penalties, apportioned to the trust;  
26 (8) disbursements related to environmental matters, including  
27 (A) reclamation;  
28 (B) assessing environmental conditions;  
29 (C) remedying and removing environmental contamination;  
30 (D) monitoring remedial activities and the release of  
31 substances;

- 1 (E) preventing future releases of substances;
- 2 (F) collecting amounts from persons liable or potentially liable
- 3 for the costs of those activities;
- 4 (G) penalties imposed under environmental statutes or
- 5 regulations and other payments made to comply with those statutes or
- 6 regulations;
- 7 (H) statutory or common law claims by third parties;
- 8 (I) defending claims based on environmental matters.

9 (b) If a principal asset is encumbered with an obligation that requires income

10 from that asset to be paid directly to the creditor, the trustee shall transfer from

11 principal to income an amount equal to the income paid to the creditor in reduction of

12 the principal balance of the obligation.

13 **Sec. 13.38.820. Discretionary allocation of disbursements.** Subject to

14 AS 13.38.800 and 13.38.810, a trustee may, in the trustee's discretion, allocate to

15 income or principal or partly to each ordinary expenses incurred in connection with

16 the administration, management, or preservation of trust property and the distribution

17 of income, including the compensation of the trustee and of a person providing

18 investment advisory, custodial, or income tax return preparation services to the trustee.

19 **Sec. 13.38.830. Transfers from income to principal for depreciation.** (a)

20 A trustee may transfer to principal a reasonable amount of the net cash receipts from a

21 principal asset that is subject to depreciation. However, a trustee may not transfer any

22 amount for depreciation

23 (1) of that portion of real property used or available for use by a

24 beneficiary as a residence or of tangible personal property held or made available for

25 the personal use or enjoyment of a beneficiary;

26 (2) during the administration of a decedent's estate; or

27 (3) under this section if the trustee is accounting under AS 13.38.620

28 for the business or activity in which the asset is used.

29 (b) An amount transferred to principal is not required to be held as a separate

30 fund.

31 (c) In this section, "depreciation" means a reduction in value due to wear, tear,

1 decay, corrosion, or gradual obsolescence of a fixed asset having a useful life of more  
2 than one year.

3 **Sec. 13.38.840. Transfers from income to reimburse principal.** (a) A  
4 trustee may transfer an appropriate amount from income to principal in one or more  
5 accounting periods to reimburse principal or to provide a reserve for future  
6 disbursements if the trustee makes or expects to make a disbursement from principal  
7 that is allocable to income under AS 13.38.800 or 13.38.820 and that is paid from  
8 principal because it is unusually large, or is made to prepare property for rental,  
9 including tenant allowances, leasehold improvements, and broker's commissions.

10 (b) If the asset whose ownership gives rise to the disbursements becomes  
11 subject to a successive income interest after an income interest ends, a trustee may  
12 continue to transfer amounts from income to principal as provided in (a) of this  
13 section.

14 (c) This section does not apply to the extent the trustee has been or expects to  
15 be reimbursed by a third party.

16 **Sec. 13.38.850. Income taxes.** (a) A tax required to be paid by a trustee  
17 based on receipts allocated to income shall be paid from income.

18 (b) A tax required to be paid by a trustee based on receipts allocated to  
19 principal shall be paid from principal, even if the tax is called an income tax by the  
20 taxing authority.

21 (c) A tax required to be paid by a trustee on the trust's share of an entity's  
22 taxable income shall be paid proportionately from

23 (1) income, to the extent that receipts from the entity are allocated to  
24 income; and

25 (2) principal, to the extent that

26 (A) receipts from the entity are allocated to principal; and

27 (B) the trust's share of the entity's taxable income exceeds the  
28 total receipts described in (1) of this subsection and (A) of this paragraph.

29 (d) For the purposes of this section, receipts allocated to principal or income  
30 shall be reduced by the amount distributed to a beneficiary from principal or income  
31 for which the trust receives a deduction in calculating the tax.

1           **Sec. 13.38.860. Adjustments between principal and income because of**  
2 **taxes.** A trustee may make adjustments between principal and income to offset the  
3 shifting of economic interests or tax benefits between income beneficiaries and  
4 remainder beneficiaries that arise from

5                   (1) an election or decision that the trustee makes regarding tax matters;

6                   (2) an income tax or any other tax that is imposed on the trustee or a  
7 beneficiary as a result of a transaction involving the trust or distribution from the trust;  
8 or

9                   (3) the ownership by a trust of an interest in an entity whose taxable  
10 income, whether or not distributed, is includable in the taxable income of the trust or a  
11 beneficiary.

#### 12                                   **Article 8. General Provisions.**

13           **Sec. 13.38.900. Not applicable to mental health trust.** This chapter does not  
14 apply to the trust established under the Alaska Mental Health Enabling Act of 1956,  
15 P.L. 84-830, 70 Stat. 709.

16           **Sec. 13.38.910. Uniformity of application and construction.** In applying  
17 and construing this chapter, consideration shall be given to the need to promote  
18 uniformity of the law with respect to its subject matter among states that enact it.

19           **Sec. 13.38.980. Definitions.** In this chapter, unless the context clearly  
20 indicates otherwise,

21                   (1) "accounting period" means a calendar year, unless another 12-  
22 month period is selected by a fiduciary, and includes a portion of a calendar year or  
23 other 12-month period that begins when an income interest begins or ends when an  
24 income interest ends;

25                   (2) "beneficiary" includes, in the case of

26                                   (A) a decedent's estate, an heir, legatee, or devisee; and

27                                   (B) a trust, an income beneficiary and a remainder beneficiary;

28                   (3) "fiduciary" means a personal representative or a trustee;

29                   (4) "income" means money or property that a fiduciary receives as  
30 current return from a principal asset, and includes a portion of receipts from a sale,  
31 exchange, or liquidation of a principal asset, to the extent provided in AS 13.38.600 -

1 13.38.740;

2 (5) "income beneficiary" means a person to whom net income of a  
3 trust is or may be payable;

4 (6) "income interest" means the right of an income beneficiary to  
5 receive all or part of net income, whether the governing instrument requires it to be  
6 distributed or authorizes it to be distributed in the trustee's discretion;

7 (7) "mandatory income interest" means the right of an income  
8 beneficiary to receive net income that the governing instrument requires the fiduciary  
9 to distribute;

10 (8) "net income" means the total receipts allocated to income during an  
11 accounting period, minus disbursements made from income during the period, and  
12 plus or minus transfers under this chapter to or from income during the period;

13 (9) "person" means an individual, a corporation, a business trust, an  
14 estate, a trust, a partnership, a limited liability company, an association, a joint  
15 venture, a government, a governmental subdivision, an agency or instrumentality, a  
16 public corporation, or another legal or commercial entity;

17 (10) "principal" means property held in trust for distribution to a  
18 remainder beneficiary when the trust terminates, or property held in trust in perpetuity;

19 (11) "remainder beneficiary" means a person entitled to receive  
20 principal when an income interest ends;

21 (12) "sui juris beneficiary" includes

22 (A) a court-appointed guardian of an incapacitated beneficiary;

23 (B) an agent for an incompetent beneficiary; and

24 (C) a court-appointed guardian of a minor beneficiary's estate;

25 (13) "trust" includes a legal life estate arrangement;

26 (14) "trustee" includes an original, additional, or successor trustee,  
27 whether or not appointed or confirmed by a court;

28 (15) "unitrust" means a trust from which a fixed percentage of the net  
29 fair market value of the trust's assets, valued annually, is paid not less often than  
30 annually to a beneficiary.

31 **Sec. 13.38.990. Short title.** This chapter may be cited as the Alaska Principal

1 and Income Act.

2 \* Sec. 3. AS 37.14.031(d) is amended to read:

3 (d) The authority shall adopt regulations providing for the determination  
4 of [PROVISIONS OF AS 13.38 APPLY TO DETERMINE] amounts attributable to  
5 [THE] principal under (b)(2) of this section. The regulations must provide for the  
6 allocation between principal and income of money received from the  
7 management of mental health trust land, and the manner of allocation must be in  
8 the long-term best interest of the trust and its beneficiaries.

9 \* Sec. 4. AS 13.38.010, 13.38.020, 13.38.030, 13.38.040, 13.38.050, 13.38.060, 13.38.070,  
10 13.38.080, 13.38.090, 13.38.100, 13.38.110, 13.38.120, 13.38.130, and 13.38.140 are  
11 repealed.

12 \* Sec. 5. The uncodified law of the State of Alaska is amended by adding a new section to  
13 read:

14 APPLICABILITY. AS 13.38.200 - 13.38.990, enacted by sec. 2 of this Act, apply,  
15 except as otherwise expressly provided in the governing instrument, and except as provided  
16 by AS 13.38.900, enacted by sec. 2 of this Act, to a trust existing on or after the effective date  
17 of this Act, and to the estate of a decedent who dies on or after the effective date of this Act.

18 \* Sec. 6. This Act takes effect September 1, 2003.

# LEGAL SERVICES

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## MEMORANDUM

March 10, 2003

**SUBJECT:** Sectional summary of SB 87, relating to the Uniform Principal and Income Act (Work Order No. 23-LS0366J)

**TO:** Senator Ralph Seekins  
Attn: Brian

**FROM:** *TLB*  
Theresa L. Bannister  
Legislative Counsel

You have requested a sectional summary of the above-described bill. As a preliminary matter, note that a sectional summary of a bill should not be considered an authoritative interpretation of the bill and the bill itself is the best statement of its contents.

Section 1. Substitutes a reference to the new principal and income chapter for a reference to the current principal and income chapter.

Section 2. Adds the new Alaska Principal and Income Act. Article 1 is entitled "Preliminary Provisions; Power to Adjust" and consists of secs. 13.38.200 - 13.38.220.

Sec. 13.38.200 provides some general guidelines for fiduciaries (personal representatives of estates and trustees) for handling the interaction between the new chapter and the instrument (e.g., will or trust document) that governs the trust or estate, and for handling the situation where the new chapter and the instrument do not provide a rule for allocating receipts and disbursements between principal and income. Directs a fiduciary to act impartially based on what is fair and reasonable to all of the beneficiaries unless the governing instrument clearly manifests an intention that the fiduciary may or shall favor a beneficiary. States that a determination in accordance with the new provisions is presumed to be fair and reasonable to all of the beneficiaries.

Sec. 13.38.210 allows a trustee to adjust between principal and income by allocating income to principal or vice versa if certain conditions are met. Lists the factors that a trustee may consider when deciding whether and to what extent to use this adjustment power. Prohibits a trustee from making an adjustment under certain listed circumstances. Allows another trustee, if there is more than one trustee, to make certain adjustments that another trustee would not be allowed to make. Allows a trustee to release the power of adjustment permanently, or for a specified period, if the trustee is uncertain whether possessing or exercising the power will cause certain results. States how to deal with a governing instrument that limits the trustee's power to adjust.

Sec. 13.28.220 prohibits a court from changing a fiduciary's decision about exercising a discretionary power under the new provisions, unless determined to be an abuse of discretion. When there is an abuse of discretion, provides for the restoration of income and remainder beneficiaries to positions they would have occupied if there hadn't been any abuse and establishes certain rules for handling the restoration.

Article 2 is entitled "Conversion to Unitrust" and consists of secs. 13.38.300 - 13.38.410.

Sec. 13.38.300 allows a trustee to release the power to adjust and convert a trust into a unitrust unless expressly prohibited by the governing instrument. Lists the conditions for when this may be done.

Sec. 13.38.310 allows a trustee to petition the court to approve a conversion of a trust to a unitrust under two conditions. Allows a beneficiary to request the conversion and to petition the court to order the conversion if the trustee does not convert. Directs a court to approve a conversion or to direct the requested conversion if court concludes the conversion will enable the trustee to better carry out the intent of the settlor or testator and the trust's purposes.

Sec. 13.38.320 lists certain factors that a trustee may consider when deciding whether to exercise the power to convert a trust to a unitrust.

Sec. 13.38.330 directs that after conversion, the trustee shall follow a specified investment policy and make certain distributions. Establishes a specific meaning for "income" in the governing instrument after conversion. Directs that after administration as a unitrust for three years, the four percent amount referred to in the meaning of "income" is to be averaged over the three preceding years.

Sec. 13.38.340 allows the trustee of a unitrust to determine certain listed items, including the effective date of the conversion, the frequency of distributions, and what valuation dates to use.

Sec. 13.38.350 provides for deduction from a unitrust distribution those expenses that would be deducted from income if the trust were not a unitrust. Unless the governing instrument provides otherwise, indicates what sources a unitrust distribution is considered to have been paid from.

Sec. 13.38.360 authorizes the trustee or a beneficiary, if the trustee declines, to petition the court to select a payout percentage, to provide for certain net income distributions, and to average the net asset valuation over a period other than three years.

Sec. 13.38.370 states that a conversion does not affect certain provisions in the governing instrument that relate to trustee distribution of principal or beneficiary withdrawal of principal.

Senator Ralph Seekins

March 10, 2003

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Sec. 13.38.380 prohibits a trustee from converting a trust into a unitrust under certain described conditions.

Sec. 13.38.390 allows another trustee to make a conversion that one trustee may not, unless prohibited by the governing instrument. Allows the trustees to petition the court to direct a conversion if certain prohibitions apply to all of the trustees.

Sec. 13.38.400 authorizes a trustee to reconvert a unitrust back into a trust by following the procedures for conversion. Restores the trustee's power to adjust when there is a reconversion.

Sec. 13.38.410 allows, under certain circumstances, a trustee to release permanently or for a specified period the power to make a conversion.

Article 3 is entitled "Charitable Trust Election" and consists of secs. 13.38.440 - 13.38.490.

Sec. 13.38.440 allows a trustee of a trust held exclusively for charitable purposes to elect to be governed by this charitable trust election article unless the governing instrument expressly prohibits this election.

Sec. 13.38.450 requires that to make the election the trustee must adopt and follow an investment policy seeking a total return for the investments held by the trust. Establishes certain formalities for adopting the policy.

Sec. 13.38.460 directs a trustee, after making a charitable trust election, to select the percentage of the value of the trust that will be considered income and determine that it is consistent with the long-term preservation of the real value of the principal of the trust. Establishes certain limitations on what the percentage may be and how often it may be changed. Establishes that for charitable trusts required by the Internal Revenue Code to distribute a higher amount than otherwise selected under this section, the distribution amount required by the Internal Revenue Code controls over the percentage selected.

Sec. 13.38.470 authorizes a trustee to revoke a charitable trust election under certain conditions. Establishes certain formalities for establishing the revocation and an alternative investment policy.

Sec. 13.38.480 establishes what the value of the trust is for the purposes of applying the charitable election provisions. Allows for averaging the value of the trust over three or more preceding years when the trust has been administered as a unitrust under this section for at least three years.

Sec. 13.38.490 defines certain terms for the provisions dealing with the charitable trust election.

Article 4 is entitled "Decedent's Estate or Terminating Income Interest" and consists of secs. 13.38.500 - 13.38.510.

Sec. 13.38.500 gives a fiduciary certain directions regarding determinations, distributions, and reductions of principal and income receipts after a decedent dies, in the case of an estate, or after an income interest in a trust ends.

Sec. 13.38.510 indicates the distributions to which certain beneficiaries identified in the previous section are entitled. Establishes certain rules for determining a beneficiary's share of net income. Requires the fiduciary to maintain certain records regarding a beneficiary's interest, if the fiduciary doesn't distribute all of the collected but undistributed net income to each person as of a distribution date. Allows the fiduciary under certain conditions to apply this section's rules to certain net gains or losses from the disposition of a principal asset. Provides for using a distribution date that is when the fiduciary calculates the value of the assets.

Article 5 is entitled "Apportionment at Beginning and End of Income Interest" and consists of secs. 13.38.550 - 13.38.570.

Sec. 13.38.550 states that an income beneficiary is entitled to net income from the date when the income interest begins and establishes when an income interest begins. States when an asset becomes subject to a trust. States when an asset becomes subject to a successive income interest. Establishes when an income interest ends.

Sec. 13.38.560 indicates when a trustee is to allocate an income receipt or disbursement to principal and when to income. Indicates when an item of income or an obligation is considered to be due.

Sec. 13.38.570 gives directions on how to proceed when a mandatory income interest ends. Gives direction to a trustee on how to handle the final payment when the trustee's obligation to pay a fixed annuity or a fixed fraction of the trust's assets' value ends.

Article 6 is entitled "Allocation of Receipts during Administration of trust" and consists of secs. 13.38.600 - 13.38.740.

Sec. 13.38.600 directs the trustee when to allocate to income money received from an entity and when to allocate entity receipts from an entity to principal. States when money is considered to have been received in partial liquidation. Indicates when a trustee may rely on an entity's statement about the source or character of a distribution. Defines "entity" for the section.

Sec. 13.38.610 indicates when the trustee is to allocate to principal or income the income from a trust or an estate in which the trust has an interest other than a purchased interest. Indicates which sections apply to receipts from certain purchased interests.

Sec. 13.38.620 allows a trustee to maintain separate accounting records for activity conducted by the trust that is in the best interest of all the beneficiaries, whether or not the assets of the activity are segregated from other trust assets. Allows the trustee who accounts separately to make certain determinations relating to its net cash receipts. Under certain circumstances directs the trustee to account in the trust's general accounting records for the net amount received as principal from a sale of the activity's assets not made in the ordinary course of the activity. Lists the activities for which a trustee may maintain separate accounting records.

Sec. 13.38.630 directs the trustee to allocate to principal certain listed receipts.

Sec. 13.38.640 directs the trustee to allocate to income certain receipts from rental property. Indicates how to handle amounts received as refundable deposits.

Sec. 13.38.650 directs the trustee to allocate to income certain money received as interest. Requires the trustee to allocate to principal certain amounts received from the sale, redemption, or other disposition of an obligation to pay money to the trustee. Indicates how to allocate certain amounts received from short-term obligations to pay money to the trustee. Indicates that this section does not apply to obligations covered by certain listed sections.

Sec. 13.38.660 provides directions to the trustee on how to allocate to principal and income certain proceeds of and certain dividends from a life insurance policy or other contract in which the trust or its trustee is named as beneficiary. Directs a trustee to allocate to income the proceeds of certain other insurance contracts.

Sec. 13.38.670 provides direction to the trustee on how to handle allocations that are insubstantial. Indicates when an allocation is presumed to be insubstantial.

Sec. 13.38.680 provides directions to the trustee on how to allocate to income and principal certain payments that a trustee may receive over a fixed period of time or during the life of one or more individuals because of services rendered or property transferred to the payor in exchange for future payments, including annuities, deferred compensation agreements, employee death benefits, individual retirement accounts, and pension plans.

Sec. 13.38.690 indicates how a trustee is to allocate between principal and income receipts from liquidating assets. Defines "liquidating asset" for the section.

Sec. 13.38.700 indicates, to the extent that a trustee accounts for receipts from an interest in minerals or other natural resources under this section, how a trustee is to allocate between principal and income receipts from minerals and other natural resources. Indicates how a trustee is to allocate between principal and income amounts received on account of an interest in renewable and nonrenewable water. States that this chapter

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applies whether or not a decedent or a donor was extracting minerals, water, or other natural resources before the interest became subject to the trust.

Sec. 13.38.710 indicates, to the extent that a trustee accounts for receipts from the sale of timber and related products under this section, how the trustee is to allocate between principal and income net receipts from the sale of timber and related products. States that this chapter applies whether or not a decedent or transferor was harvesting timber from the property before it became subject to the trust.

Sec. 13.38.720 allows a spouse to require a trustee to make certain trust property productive of income, convert the property within a reasonable time, or to exercise the power of adjustment under sec. 13.38.210(a) under certain circumstances related to federal estate or gift tax marital deductions. Indicates that for cases not governed by (a) of this section, proceeds from the sale or other disposition of an asset are principal without regard to the amount of income the asset produces during any accounting period.

Sec. 13.38.730 indicates that, to the extent that a trustee does not account under sec. 13.38.620 for transactions in derivatives, the trustee is to allocate to principal receipts from, and disbursements made, in connection with transactions in derivatives. Allocates to principal certain amounts related to options. Defines "derivative" for the section.

Sec. 13.38.740. Directs the trustee on how to allocate between principal and income payments from interest, or other current return, and from other proceeds of collateral financial assets. Directs the trustee on how to allocate between principal and income those payments received in exchange for the trust's entire interest in an asset-backed security. Defines "asset-backed security" for the section.

Article 7 is entitled "Allocation of Disbursements During Administration of Trust" and consists of secs. 13.38.800 - 13.38.860.

Sec. 13.38.800 requires a trustee to make certain listed disbursements from income.

Sec. 13.38.810 requires a trustee to make certain listed disbursements from principal.

Sec. 13.38.820 allows the trustee, in the trustee's discretion, to allocate, subject to AS 13.38.800 - 13.38.810, to income or principal ordinary expenses incurred in the administration, management, or preservation of trust property and the distribution of income.

Sec. 13.38.830 authorizes a trustee to transfer to principal a reasonable amount of the net cash receipts from a principal asset that is subject to depreciation. Lists certain exceptions. States that an amount transferred to principal is not required to be held as a separate fund.

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Sec. 13.38.840 authorizes a trustee to transfer an appropriate amount from income to principal in order to reimburse principal or to provide a reserve for future disbursements under certain conditions. Allows for continuing the transfers from income to principal under certain conditions. States that this section does not apply to the extent the trustee has been or expects to be reimbursed by a third party.

Sec. 13.38.850 directs that a tax required to be paid by a trustee based on receipts allocated to income is to be paid from income. Directs that a tax required to be paid by a trustee based on receipts allocated to principal is to be paid from principal. Indicates how the payment of a tax required to be paid on the trust's share of an entity's taxable income is to be allocated between principal and income.

Sec. 13.38.860 allows a trustee to make adjustments between principal and income to offset the shifting of economic interests or tax benefits between income beneficiaries and remainder beneficiaries arising from certain listed factors.

Sec. 13.38.900 requires that when applying these new provisions consideration be given to the need to promote uniformity among the state enacting these provisions.

Sec. 13.38.980 defines certain terms for the new provisions.

Sec. 13.38.990 gives the new provisions the name of "Alaska Principal and Income Act."

Section 3. Repeals the current chapter entitled "Principal and Income of Trusts."

Section 4. States to which trusts and estates, the new principal and income provisions apply.

Section 5. Makes this Act effective September 1, 2003.

If I may be of further assistance, please advise.

TLB:mdr

03-028.mdr

LAW OFFICES OF  
DAVID G. SHAFTELA PROFESSIONAL CORPORATION  
550 West Seventh Avenue, Suite 705  
Anchorage, Alaska 99501

(907) 276-6015

FAX (907) 278-6015

E-MAIL: info@shafteclaw.com

www.shafteclaw.com

Legal Assistants:Linda J. Durr, PLS  
Jack Jacobs+ Admitted in AK  
+ Admitted in CA  
+ Admitted in WAAttorneys:David G. Shafteclaw, J.D., LL.M. (Taxation)++  
Charles F. Schutze, J.D., LL.M. (Taxation)+  
Caroline P. Wannmaker, J.D.++  
Donna Marie, J.D.+  
Bhrec Roumagoux, J.D.+

December 31, 2002

Senator Ralph Seekins  
Seekins Ford Lincoln  
1625 Old Steese Highway  
Fairbanks, AK 99709**Re: Introduction of the Uniform Principal and Income Act**

Dear Senator Seekins:

I am a member of an informal group of trust and estate attorneys who annually review legislation that would be advantageous for the State of Alaska in this area. We recommend that the Alaska Legislature consider and adopt the Pennsylvania version of the 1997 Uniform Principal and Income Act.

In 2002, Pennsylvania adopted the 1997 Uniform Principal and Income Act, with some significant changes. These include a power to convert to a unitrust and a number of other significant provisions. Also in 2002 the State of Washington adopted Pennsylvania's version of the Uniform Principal and Income Act.

Enclosed is the full report of the Advisory Committee on the Pennsylvania version of the Uniform Principal and Income Act. This report includes the various sections of the Uniform Act, the Uniform Commission's comments and, where Pennsylvania has changed the Act, additional Pennsylvania comments describing these changes.

I have conferred with several of the attorneys who participated in the Advisory Committee for the Pennsylvania version of the Act. They have recommended the following additional changes.

1. Section 8102, relating to definitions.
2. Section 8105(a)(2) and (3), relating to notice.
3. Section 8105(d)(3), relating to calculation of the unitrust amount.
4. Section 8105 [new letter subsection], relating to reconversion.

I have included all of the above changes.

Senator Ralph Seekins  
December 31, 2002  
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Thank you very much for agreeing to sponsor this Act. This updating of the Uniform Principal and Income Act will facilitate the administration of Alaska trusts, and therefore provide significant benefits to the residents of our state.

Sincerely,



David G. Shaftel

Enclosures: As stated

Terry Kerty  $\approx$

Co.	Wave Skattel
Co.	
Dept.	Phone #
Fax # 907 465-5241	Fax # 907 278-6015



## Uniform Law Commissioners

The National Conference of Commissioners on Uniform State Laws

Section Title: Introductions & Adoptions Of Uniform Acts.

### > Why States Should Adopt the ...

#### UNIFORM PRINCIPAL AND INCOME ACT (1997)

The Uniform Principal and Income Act, originally promulgated by the Uniform Law Commissioners in 1931, revised in 1962, and adopted in 41 states, provides procedures for trustees administering an estate in separating principal from income. The basic purpose of the new act, like the 1931 and 1962 versions, is to ensure that the intention of the trust creator is the guiding principle for trustees.

Like its predecessors, this revision distinguishes between property that is principal, which will be distributed to remainder beneficiaries (persons entitled to receive principal when an income interest ends), and property that is income distributed to income beneficiaries.

The Uniform Act has always provided the default rules for such allocations in the event the trust investment is silent.

There are many reasons why every state should adopt the Revised Uniform Principal and Income Act (1997).

- The law of trust investment has been modernized. It is now time to update the traditional allocation rules so that it can work with the doctrine of modern investment theory.
- The new act provides a means for implementing the transition to an investment regime based on principles embodied in the Uniform Prudent Investor Act, especially the principle for investing for total return instead of for a certain level of income.
- The new act better clarifies allocations of acquired assets, such as those from corporate distributions.
- An "unincorporated entity" concept has been introduced to deal with businesses operated by a trustee, including farming and livestock operations, and investment activities in rental real estate, natural resources, and timber.
- The new act provides for investment modalities that were not in existence in 1962, such as derivatives, options, deferred payment obligations, and synthetic financial assets.
- There is a new provision which deals with the problem of disbursements made because of environmental laws.
- New provisions which deal with the imbalances as a result of tax laws are also included. The act provides the power to make adjustments between principal and income to correct inequities caused by tax elections or peculiarities in the way the fiduciary income tax rules apply.

#### UNIFORMITY

This act will provide uniformity of law, necessary in an interstate investment environment. The Revised Uniform Principal and Income Act provides answers to long-standing problems in reconciling modern portfolio management with traditional rules of income allocation. It is important that every state adopt this act as soon as possible.

# FISCAL NOTE

STATE OF ALASKA  
2003 LEGISLATIVE SESSION

Fiscal Note Number: 1  
Bill Version: SB 87  
(S) Publish Date: 4/15/03

Revision Date/Time (Note if correction): \_\_\_\_\_ Dept. Affected: Law  
Title "An Act relating to principal and income in the BRU Civil Division  
administration of trusts and decedents' estates . . ." Component Commercial  
Sponsor Senator Seekins  
Requester Senate Judiciary Committee Component No. 2211

**Expenditures/Revenues** (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
<b>TOTAL OPERATING</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

<b>CAPITAL EXPENDITURES</b>						
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<b>CHANGE IN REVENUES ( )</b>						
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**FUND SOURCE** (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type-Do not abbreviate)						
<b>TOTAL</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

Estimate of any current year (FY2003) cost: 0.0  
Check this box (X) if funding for this bill is included in the Governor's FY 2004 budget proposal:

**POSITIONS**

Full-time						
Part-time						
Temporary						

**ANALYSIS:** (Attach a separate page if necessary)

This bill would bring current the Uniform Principal and Income Act, which provides rules for the determination of whether a trust's or estate's receipts should be considered income or principal, by adopting the 1997 version of the Act.

Passage of this legislation will have no fiscal impact on the Department of Law.

Prepared by: Joan M. Kasson Phone (907) 465-5370  
Division Attorney General's Office Date/Time 4/14/03 12:57 PM  
Approved by: Joan M. Kasson for Gregg D. Renkes, Attorney General Date 4/14/2003  
Agency Department of Law