

GENERAL ASSEMBLY OF NORTH CAROLINA  
SESSION 2005

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SENATE BILL 461

Short Title: Unitrust Amendments.

(Public)

Sponsors: Senator Hartsell.

Referred to: Judiciary II.

March 10, 2005

1 A BILL TO BE ENTITLED  
2 AN ACT TO AMEND THE LAW RELATING TO UNITRUSTS.  
3 The General Assembly of North Carolina enacts:

4 **SECTION 1.** G.S. 37A-1-104.1(5) reads as rewritten:

5 "(5) "Income trust" means a trust, created by either an inter vivos or a  
6 testamentary instrument, which directs or permits the trustee to  
7 distribute the net income of the trust to one or more persons, either in  
8 fixed proportions or in amounts or proportions determined by the  
9 trustee. ~~Notwithstanding the foregoing, no trust that may be subject to~~  
10 ~~taxation under section 2001 or section 2501 of the Code shall be an~~  
11 ~~income trust for purposes of this Part, until the expiration of the period~~  
12 ~~for filing the return therefor, including all extensions for the filing.~~  
13 trustee, and regardless of whether the trust directs or permits the  
14 trustee to distribute principal of the trust to one or more of those  
15 persons."

16 **SECTION 2.** G.S. 37A-1-104.1 is amended by adding a new subdivision to  
17 read:

18 "(9a) "Treasury Regulations" means the regulations, rulings, procedures,  
19 notices, or other administrative pronouncements issued by the Internal  
20 Revenue Service, as amended from time to time."

21 **SECTION 3.** G.S. 37A-1-104.2 reads as rewritten:

22 **"§ 37A-1-104.2. Conversion in trustee's discretion without court approval.**

23 (a) Any trustee, other than an interested trustee, or, where two or more persons  
24 are acting as trustees, a majority of the trustees who are not interested trustees (in either  
25 case hereafter "trustee"), may, in the trustee's sole discretion and without court approval,  
26 (i) convert an income trust to a total return unitrust, (ii) reconvert a total return unitrust  
27 to an income trust, or (iii) change the percentage used to calculate the unitrust amount or  
28 the method used to determine the fair market value of the trust if:

- 1           (1) The trustee adopts a written policy for the trust providing (i) in the  
2 case of a trust being administered as an income trust, that future  
3 distributions from the trust will be unitrust amounts rather than net  
4 income, (ii) in the case of a trust being administered as a total return  
5 unitrust, that future distributions from the trust will be net income  
6 rather than unitrust amounts, or (iii) that the percentage used to  
7 calculate the unitrust amount or the method used to determine the fair  
8 market value of the trust will be changed as stated in the policy;
- 9           (2) The trustee sends written notice of its intention to take the action,  
10 along with copies of the written policy and this Part, to (i) the grantor  
11 of the trust, if living, (ii) all the competent beneficiaries who are  
12 currently receiving or eligible to receive distributions of income of the  
13 trust, (iii) without regard to the exercise of a general power of  
14 appointment, all competent beneficiaries who would receive or be  
15 eligible to receive the distributions of income of the trust if the  
16 interests of the beneficiaries currently receiving or eligible to receive  
17 the income terminated at the time of the giving of the notice but the  
18 termination of those interests would not cause the trust to terminate,  
19 (iv) without regard to the exercise of any power of appointment, all the  
20 competent beneficiaries who would receive principal of the trust if the  
21 trust were to terminate at the time of the giving of the notice ~~(without~~  
22 ~~regard to the exercise of any power of appointment)~~ notice, and (iv) (v)  
23 all persons acting as advisor or protector of the trust;
- 24           (3) ~~There is at least one competent beneficiary who is currently receiving~~  
25 ~~or eligible to receive distributions of income of the trust and there is at~~  
26 ~~least one competent beneficiary who would receive principal of the~~  
27 ~~trust if the trust were to terminate at the time of the giving of the~~  
28 ~~notice; There is at least one competent beneficiary described in~~  
29 ~~subsection (a)(2)(ii) or subsection (a)(2)(iii) of this section and one~~  
30 ~~competent beneficiary described in subsection (a)(2)(iv) of this~~  
31 ~~section; and~~
- 32           (4) No person receiving notice of the trustee's intention to take the  
33 proposed action of the trustee objects to the action within 60 days of  
34 receipt of the notice by written instrument delivered to the trustee.
- 35           (b) If there is no trustee of the trust other than an interested trustee, the interested  
36 trustee or, where two or more persons are acting as trustee and are interested trustees, a  
37 majority of the interested trustees may, in its sole discretion and without court approval,  
38 (i) convert an income trust to a total return unitrust, (ii) reconvert a total return unitrust  
39 to an income trust, or (iii) change the percentage used to calculate the unitrust amount or  
40 the method used to determine the fair market value of the trust if:
- 41           (1) The trustee adopts a written policy for the trust providing (i) in the  
42 case of a trust being administered as an income trust, that future  
43 distributions from the trust will be unitrust amounts rather than net  
44 income as determined under this Chapter, (ii) in the case of a trust

1 being administered as a total return unitrust, that future distributions  
2 from the trust will be net income as determined under this Chapter  
3 rather than unitrust amounts, or (iii) that the percentage used to  
4 calculate the unitrust amount or the method used to determine the fair  
5 market value of the trust will be changed as stated in the policy;

6 (2) The trustee appoints a disinterested person who, in its sole discretion  
7 but acting in a fiduciary capacity, determines for the trustee (i) the  
8 percentage to be used to calculate the unitrust amount, (ii) the method  
9 to be used in determining the fair market value of the trust, and (iii)  
10 which assets, if any, are to be excluded in determining the unitrust  
11 amount;

12 (3) The trustee sends written notice of its intention to take the action,  
13 along with copies of the written policy and this Part, and the  
14 determinations of the disinterested person to (i) the grantor of the trust,  
15 if living, (ii) all the competent beneficiaries who are currently  
16 receiving or eligible to receive distributions of income of the trust, (iii)  
17 without regard to the exercise of a general power of appointment, all  
18 competent beneficiaries who would receive or be eligible to receive  
19 the distributions of income of the trust if the interests of the  
20 beneficiaries currently receiving or eligible to receive the income  
21 terminated at the time of the giving of the notice but the termination of  
22 those interests would not cause the trust to terminate, (iv) without  
23 regard to the exercise of any power of appointment, all the competent  
24 beneficiaries who would receive principal of the trust if the trust were  
25 to terminate at the time of the giving of the notice (without regard to  
26 the exercise of any power of appointment) notice, and (iv) (v) all  
27 persons acting as advisor or protector of the trust;

28 (4) ~~There is at least one competent beneficiary who is currently receiving~~  
29 ~~or eligible to receive distributions of income of the trust and there is at~~  
30 ~~least one competent beneficiary who would receive principal of the~~  
31 ~~trust if the trust were to terminate at the time of the giving of the~~  
32 ~~notice; There is at least one competent beneficiary described in~~  
33 ~~subsection (b)(3)(ii) or subsection (b)(3)(iii) of this section and one~~  
34 ~~competent beneficiary described in subsection (b)(3)(iv) of this~~  
35 ~~section; and~~

36 (5) No person receiving notice of the trustee's intention to take the  
37 proposed action of the trustee objects to the action or to the  
38 determination of the disinterested person within 60 days of receipt of  
39 the notice by written instrument delivered to the trustee.

40 (c) A trustee may act pursuant to subsection (a) or (b) of this section with respect  
41 to a trust for which both income and principal have been permanently set aside for  
42 charitable purposes under the governing instrument and for which a federal estate or gift  
43 tax deduction has been taken, provided that:

- 1           (1) Instead of sending written notice to the persons described in  
2           subsections (a)(2) and (3) of this section or subsections (b)(2) and (3)  
3           of this section, as the case may be, the trustee shall send such written  
4           notice to the named charity or charities then entitled to receive income  
5           of the trust and, if no named charity or charities are entitled to receive  
6           all of the income, to the Attorney General of this State;  
7           (2) Subsection (a)(4) or subsection (b)(4) of this section, as the case may  
8           be, shall not apply to such action; and  
9           (3) In each taxable year, the trustee shall distribute the greater of the  
10           unitrust amount and the amount required by section 4942 of the Code."

11           **SECTION 4.** G.S. 37A-1-104.4 reads as rewritten:

12           "**§ 37A-1-104.4. Determination of unitrust amount.**

13           (a) The fair market value of the trust shall be determined at least annually, using  
14 a valuation date selected by the trustee in its discretion. The trustee, in its discretion,  
15 may use an average of the fair market value on the same valuation date for the current  
16 fiscal year and not more than three preceding fiscal years, if the use of this average  
17 appears desirable to reduce the impact of fluctuations in market value on the unitrust  
18 amount. Assets for which a fair market value cannot be readily ascertained shall be  
19 valued using valuation methods as are considered reasonable and appropriate by the  
20 trustee. ~~These assets may be excluded from valuation, provided all income received~~  
21 ~~with respect to these assets is distributed to the extent distributable in accordance with~~  
22 ~~the terms of the governing instrument. Assets used by the trust beneficiary, such as a~~  
23 ~~residence or tangible personal property, may also be excluded from the fair market~~  
24 ~~value for computing the unitrust amount.~~

25           (b) The percentage to be used in determining the unitrust amount shall be a  
26 reasonable current return from the trust, in any event not less than three percent (3%)  
27 nor more than five percent (5%), taking into account the intentions of the grantor of the  
28 trust as expressed in the governing instrument, the needs of the beneficiaries, general  
29 economic conditions, projected current earnings and appreciation for the trust, and  
30 projected inflation and its impact on the trust.

31           ~~(c) In the case of a trust (i) for which a marital deduction has been taken for~~  
32 ~~federal tax purposes under section 2056 or section 2523 of the Code (during the lifetime~~  
33 ~~of the spouse for whom the trust was created) or (ii) a trust to which the~~  
34 ~~generation-skipping transfer tax due under section 2601 of the Code does not apply by~~  
35 ~~reason of any effective date or transition rule, the unitrust amount in any taxable year~~  
36 ~~shall not be less than the net income of the trust, determined without regard to~~  
37 ~~subsection (d) of this section.~~

38           (d) Following the conversion of an income trust to a total return unitrust, the  
39 trustee:

- 40           (1) ~~Shall treat the unitrust amount as if it were net income of the trust for~~  
41 ~~purposes of determining the amount available, from time to time, for~~  
42 ~~distribution from the trust; and~~  
43           (2) ~~May allocate to trust income for each taxable year of the trust (or~~  
44 ~~portion of that year) (i) net short term capital gain described in section~~

1 ~~1222(5) of the Code for that year or portion of that year, but only to~~  
2 ~~the extent that the amount allocated together with all other amounts~~  
3 ~~allocated to trust income for that year or portion of that year does not~~  
4 ~~exceed the unitrust amount for that year or portion of that year; and (ii)~~  
5 ~~net long-term capital gain described in section 1222(7) of the Code for~~  
6 ~~that year or portion of that year, but only to the extent that the amount~~  
7 ~~allocated together with all other amounts, including amounts described~~  
8 ~~in clause (i) above, allocated to trust income for that year or portion of~~  
9 ~~that year does not exceed the unitrust amount for that year or portion~~  
10 ~~of that year.~~

- 11 (1) Shall consider the unitrust amount as paid from net accounting income  
12 determined as if the trust were not a unitrust;  
13 (2) Shall then consider the unitrust amount as paid from ordinary income  
14 not allocable to net accounting income;  
15 (3) May, in the trustees discretion, consider the unitrust amount as paid  
16 from net short-term gain described in section 1222(5) of the Code and  
17 then from net long-term capital gain described in section 1222(7) of  
18 the Code so long as the discretionary power is exercised consistently  
19 and in a reasonable and impartial manner, but the amount so paid from  
20 net capital gains may not be greater than the excess of the unitrust  
21 amount over the amount of distributable net income as defined in  
22 section 643(a) of the Code without regard to section 1.643(a)-3(b) of  
23 the Treasury Regulations, as amended from time to time; and  
24 (4) Shall then consider the unitrust amount as coming from the principal  
25 of the trust."

26 **SECTION 5.** G.S. 37A-1-104.9 reads as rewritten:

27 **"§ 37A-1-104.9. Applicability.**

28 This Part shall apply to all trusts in existence on, or created after January 1, 2004,  
29 unless (i) the governing instrument contains a provision clearly expressing the grantor's  
30 intention that the current beneficiary or beneficiaries are to receive an amount other than  
31 a reasonable current return from the trust, (ii) the trust is a trust described in section  
32 170(f)(2)(B), section 664(d), section 2702(a)(3), or section 2702(b) of the Code, (iii)  
33 ~~one or more persons to whom the trustee could distribute income has a power of~~  
34 ~~withdrawal over the trust that is not subject to an ascertainable standard under section~~  
35 ~~2041 or section 2514 of the Code, or the power of withdrawal can be exercised to~~  
36 ~~discharge a duty of support the person possesses, or the trust is a trust pursuant to which~~  
37 any amount is, or has been in the past, permanently set aside for charitable purposes  
38 unless the income therefrom is also permanently devoted to charitable purposes, or (iv)  
39 the governing instrument expressly prohibits use of this Part by specific reference to this  
40 Part. Part, or expressly states the grantor's intent that net income not be calculated as a  
41 unitrust amount. A provision in the governing instrument that 'the provisions of Part 2  
42 of Article 1 of Chapter 37A or any corresponding provision of future law, shall not be  
43 used in the administration of this trust.' or 'the trustee shall not determine the

1 distributions to the income beneficiary as a unitrust amount.' or similar words reflecting  
2 such intent shall be sufficient to preclude the use of this Part."

3 **SECTION 6.** Chapter 37A of the General Statutes is amended by adding a  
4 new Part to read:

5 "Part 2A. Express Total Return Unitrusts.

6 **"§ 37A-1-104A.1. Definitions.**

7 (a) An "express total return unitrust" means a trust which by its governing  
8 instrument requires the distribution at least annually of a unitrust amount equal to a  
9 fixed percentage of not less than three percent (3%) nor more than five percent (5%) per  
10 year of the net fair market value of the trusts assets, valued at least annually.

11 (b) "Code" means the Internal Revenue Code as described in  
12 G.S. 37A-1-104.1(1).

13 (c) "Treasury Regulations" means the Treasury Regulations described in  
14 G.S. 37A-1-104.1(9a).

15 **"§ 37A-1-104A.2. Determination of unitrust amount.**

16 (a) The unitrust amount to be distributed by the express total return unitrust may  
17 be determined in the governing instrument by reference to the net fair market value of  
18 the trust's assets determined annually or averaged on a multiple year basis.

19 (b) The terms of the governing instrument of an express total return unitrust may  
20 provide that:

21 (1) Assets for which a fair market value cannot be readily ascertained shall  
22 be valued using valuation methods as are considered reasonable and  
23 appropriate by the trustee.

24 (2) Assets used by the trust beneficiary entitled to the unitrust amount,  
25 such as a residence property or tangible personal property, may be  
26 excluded from the net fair market value for computing the unitrust  
27 amount.

28 **"§ 37A-1-104A.3. Effect of distribution of unitrust amount.**

29 The distribution from an express total return unitrust of the fixed percentage of not  
30 less than three percent (3%) nor more than five percent (5%) reasonably apportions  
31 between the income beneficiaries and remaindermen the total return of an express total  
32 return unitrust.

33 **"§ 37A-1-104A.4. Change or conversion of unitrust amount.**

34 (a) The terms of the governing instrument of an express total return unitrust may  
35 provide the method similar to the method provided under G.S. 37A-1-104.2(a) for  
36 changing the unitrust percentage or for converting from a unitrust to an income trust or  
37 for a reconversion of an income trust to a unitrust, or for all of these actions.

38 (b) If the terms of the governing instrument of an express total return unitrust do  
39 not specifically or by reference to G.S. 37A-1-104.2 grant a power to the trustee to  
40 change the unitrust percentage or change to an income trust, the trustee shall have no  
41 such power.

42 **"§ 37A-1-104A.5. Determination of character of unitrust amount.**

43 Unless the terms of the governing instrument of the express total return unitrust  
44 specifically provide otherwise, the trustee:

- 1           (1) Shall consider the unitrust amount as paid from net accounting income  
2           determined as if the trust were not a unitrust;  
3           (2) Shall then consider the unitrust amount as paid from ordinary income  
4           not allocable to net accounting income;  
5           (3) May, in the trustee's discretion, consider the unitrust amount as paid  
6           from net short-term gain described in section 1222(5) of the Code and  
7           then from net long-term capital gain described in section 1222(7) of  
8           the Code so long as such discretionary power is exercised consistently  
9           and in a reasonable and impartial manner, but the amount so paid from  
10           net capital gains may not be greater than the excess of the unitrust  
11           amount over the amount of distributable net income as defined in  
12           section 643(a) of the Code without regard to section 1.643(a)-3(b) of  
13           the Treasury Regulations; and  
14           (4) Shall then consider the unitrust amount as coming from the principal  
15           of the trust.

16 **"§ 37A-104A.6. Unitrust amount in excess of a five percent payout.**

17       A trust that provides for a fixed percentage payout in excess of five percent (5%) per  
18       year shall be deemed to be an express total return unitrust that pays out a fixed  
19       percentage of five percent (5%) per year and pays out principal to the extent that the  
20       fixed percentage payout exceeds five percent (5%) per year."

21       **SECTION 7.** This act is effective when it becomes law, except that the  
22       amendment to G.S. 37A-1-104.9(iii) applies retroactively to October 1, 2004.