

PROPOSED UNITRUST CONVERSION STATUTE

KSA 58-9-105. Power to convert to unitrust.

(a) **Conversion.** Unless expressly prohibited by the governing instrument, a trustee may release the power under section KSA 58-9-104 and convert a trust into a unitrust as described in this section if all of the following apply:

- (1) The trustee determines that the conversion will enable the trustee to better carry out the intent of the settlor or testator and the purposes of the trust.
- (2) The trustee gives to each qualified beneficiary of the trust as defined by K.S.A. 58a-103(12) written notice of (A) the trustee's intention to release the power to adjust and to convert the trust into a unitrust and (B) how the unitrust will operate, including what initial decisions the trustee will make under this section.
- (3) No qualified beneficiary objects to the conversion to a unitrust in a writing delivered to the trustee within 60 days of the mailing of the notice under subsection (a)(2).

(b) **Judicially approved conversion.**

- (1) If a qualified beneficiary timely objects to the conversion to a unitrust, the trustee may petition the court to approve the conversion to a unitrust.
- (2) A qualified beneficiary may request a trustee to convert to a unitrust. If the trustee does not convert, the qualified beneficiary may petition the court to order the conversion.
- (3) The court shall approve the conversion or direct the requested conversion if the court concludes that the conversion will enable the trustee to better carry out the intent of the settlor or testator and the purposes of the trust, after considering the factors enumerated under subsection (c) deemed by the court to be relevant.

(c) **Factors.** In deciding whether to exercise the power conferred by subsection (a), the trustee shall consider all factors relevant to the trust and its beneficiaries, including the following to the extent they are relevant:

- (1) The nature, purpose, and expected duration of the trust;
- (2) the intent of the settlor;

- 1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
41
- (3) the identity and circumstances of the beneficiaries;
 - (4) the needs for liquidity, regularity of income, and preservation and appreciation of capital;
 - (5) the assets held in the trust; the extent to which they consist of financial assets, interests in closely held enterprises, tangible and intangible personal property, or real property; the extent to which an asset is used by a qualified beneficiary; and whether an asset was purchased by the trustee or received from the settlor;
 - (6) the net amount allocated to income under the other sections of this act and the increase or decrease in the value of the principal assets, which the trustee may estimate as to assets for which market values are not readily available;
 - (7) the actual and anticipated effect of economic conditions on principal and income and effects of inflation and deflation; and
 - (8) the anticipated tax consequences of conversion.
- (d) **Post conversion.** After a trust is converted to a unitrust, all of the following apply:
- (1) The trustee shall follow an investment policy seeking a total return for the investments held by the trust, whether the return is to be derived:
 - (A) from appreciation of capital;
 - (B) from earnings and distributions from capital; or
 - (C) from both.
 - (2) The trustee shall make regular distributions in accordance with the governing instrument construed in accordance with the provisions of this section.
 - (3) The term “income” in the governing instrument shall mean an annual distribution (the unitrust distribution) equal to between three percent (3%) and five percent (5%) (the payout percentage) of the net fair market value of the trust’s assets, whether such assets would be considered income or principal under other provisions of this act, averaged over a period of up to the three (3) preceding years.

- 1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
- (e) **Discretion of trustee.** The trustee may, in the trustee's discretion from time to time, determine all of the following:
- (1) The effective date of a conversion to a unitrust.
 - (2) The provisions for prorating a unitrust distribution for a short year in which a qualified beneficiary's right to payments commences or ceases.
 - (3) The frequency of unitrust distributions during the year.
 - (4) The effect of other payments from or contributions to the trust on the trust's valuation.
 - (5) Whether to value the trust's assets annually or more frequently.
 - (6) What valuation dates to use.
 - (7) How frequently to value nonliquid assets and whether to estimate their value.
 - (8) Whether to omit from the calculations trust property occupied or possessed by a qualified beneficiary.
 - (9) Any other matters necessary for the proper functioning of the unitrust.
- (f) **Allocation.**
- (1) Expenses which would be deducted from income if the trust were not a unitrust may not be deducted from the unitrust distribution.
 - (2) Unless otherwise provided by the governing instrument, the unitrust distribution shall be paid from the following sources in the following order: net income, net realized short-term capital gains, net realized long-term capital gains and the principal of the trust.
- (g) **Court orders.** The trustee or, if the trustee declines to do so, a qualified beneficiary may petition the court to:
- (1) Authorize a payout percentage of less than three percent or more than five percent.

- 1 (2) Provide for a distribution of net income, as would be determined if the trust
2 were not a unitrust, in excess of the unitrust distribution if such distribution
3 is necessary to preserve a tax benefit.
4
- 5 (3) Average the valuation of the trust's net assets over a period other than three
6 years.
7
- 8 (4) Reconvert from a unitrust. Upon a reconversion, the power to adjust under
9 KSA 58-9-104 shall be revived.
10
- 11 (h) **Application.** A conversion to a unitrust does not affect a provision in the governing
12 instrument directing or authorizing the trustee to distribute principal or authorizing
13 a qualified beneficiary to withdraw a portion or all of the principal.
14
- 15 (i) **Prohibited conversions.** Except as provided in subsection (j), a trust may not be
16 converted into a unitrust in any of the following circumstances:
17
 - 18 (1) If payment of the unitrust distribution would change the amount payable to
19 a qualified beneficiary as a fixed annuity or a fixed fraction of the value of
20 the trust assets.
21
 - 22 (2) If the unitrust distribution would be made from any amount which is
23 permanently set aside for charitable purposes under the governing instrument
24 and for which a Federal estate or gift tax deduction has been taken, unless
25 both income and principal are so set aside.
26
 - 27 (3) If:
28
 - 29 (A) possessing or exercising the power to convert would cause an
30 individual to be treated as the owner of all or part of the trust for
31 Federal income tax purposes; and
32
 - 33 (B) the individual would not be treated as the owner if the trustee did not
34 possess the power to convert.

- 1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28
29
30
31
32
33
34
35
36
37
38
39
40
- (4) If:
 - (A) possessing or exercising the power to convert would cause all or part of the trust assets to be subject to Federal estate or gift tax with respect to an individual; and
 - (B) the assets would not be subject to Federal estate or gift tax with respect to the individual if the trustee did not possess the power to convert.
 - (5) If the conversion would result in the disallowance of a Federal estate tax or gift tax marital deduction which would be allowed if the trustee did not have the power to convert.
 - (6) If the trustee is a qualified beneficiary of the trust.
 - (j) **Permissible conversion when otherwise prohibited.**
 - (1) If subsection(i)(3), (4) or (6) applies to a trustee and there is more than one trustee, a co-trustee to whom the provision does not apply may convert the trust unless the exercise of the power by the remaining trustee or trustees is prohibited by the governing instrument.
 - (2) If subsection (i)(3), (4) or (6) applies to all the trustees, the trustees may petition the court to direct a conversion.
 - (k) **Release of the power to convert.**
 - (1) A trustee may release the power conferred by subsection (a) to convert to a unitrust if any of the following apply:
 - (A) The trustee is uncertain about whether possessing or exercising the power will cause a result described in subsection (i)(3), (4) or (5).
 - (B) The trustee determines that possessing or exercising the power will or may deprive the trust of a tax benefit or impose a tax burden not described in subsection (i).
 - (2) The release may be permanent or for a specified period, including a period measured by the life of an individual.

COMMENT

1
2
3 The proposed unitrust conversion statute is patterned after Pennsylvania statute 20 Pa.
4 C.S.A. § 8105. The Pennsylvania statute has been slightly changed by the Kansas drafting
5 Committee.
6

7 The proposed Kansas statute refers to "qualified beneficiary" as defined by K.S.A. 58a-
8 103(12) and in subsection (c), the considerations in deciding whether to exercise the power to
9 convert a trust into a unitrust contained in the Pennsylvania statute have been replaced by factors
10 (1) through (6) and (8) and (9) of K.S.A. 58-9-104. The payment percentage of five percent in the
11 Pennsylvania statute has been replaced by a range of three to five percent (which is patterned after
12 the Missouri statute). Instead of using the Pennsylvania language that net market value will be
13 calculated over the lesser of the preceding three years, or the period during which the trust has been
14 in existence, uses language that allows the net market value to be calculated over a period of up to
15 the three preceding years. Other changes are minor and technical in nature.
16

17 It is suggested that the new statute become a part of the Uniform Principal and Income Act
18 (K.S.A. 58-9-102 *et seq.*) at new section 58-9-105.
19
20
21
22