

AN ACT

RELATING TO TRUSTS; AMENDING AND ENACTING CERTAIN SECTIONS OF
THE UNIFORM PRINCIPAL AND INCOME ACT.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF NEW MEXICO:

Section 1. Section 46-3A-102 NMSA 1978 (being Laws
2001, Chapter 113, Section 102) is amended to read:

"46-3A-102. DEFINITIONS.--As used in the Uniform
Principal and Income Act:

A. "accounting period" means a calendar year
unless another twelve-month period is selected by a fiduciary.
The term includes a portion of a calendar year or other
twelve-month period that begins when an income interest begins
or ends when an income interest ends;

B. "beneficiary" includes, in the case of a
decedent's estate, an heir and devisee and, in the case of a
trust, an income beneficiary and a remainder beneficiary;

C. "fiduciary" means a personal representative or
a trustee. The term includes an executor, administrator,
successor personal representative, special administrator and a
person performing substantially the same function;

D. "income" means money or property that a
fiduciary receives as current return from a principal asset.
The term includes a portion of receipts from a sale, exchange
or liquidation of a principal asset, to the extent provided in

Article 4 of the Uniform Principal and Income Act;

E. "income beneficiary" means a person to whom net income of a trust is or may be payable;

F. "income interest" means the right of an income beneficiary to receive all or part of net income, whether the terms of the trust require it to be distributed or authorize it to be distributed in the trustee's discretion;

G. "mandatory income interest" means the right of an income beneficiary to receive net income that the terms of the trust require the fiduciary to distribute;

H. "net income" means the total receipts allocated to income during an accounting period minus the disbursements made from income during the period, plus or minus transfers under the Uniform Principal and Income Act to or from income during the period;

I. "person" means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, government; governmental subdivision, agency or instrumentality; public corporation; or any other legal or commercial entity;

J. "principal" means property held in trust for distribution to a remainder beneficiary when the trust terminates;

K. "qualified beneficiary" means a beneficiary who, on the date the beneficiary's qualification is

determined:

(1) is a distributee or a permissible distributee of trust income or principal;

(2) would be a distributee or permissible distributee of trust income or principal if the interest of the distributees described in Paragraph (1) of this subsection terminated on that date; or

(3) would be a distributee or permissible distributee of trust income or principal if the trust terminated on that date;

L. "remainder beneficiary" means a person entitled to receive principal when an income interest ends;

M. "terms of a trust" means the manifestation of the intent of a settlor or decedent with respect to the trust, expressed in a manner that admits of its proof in a judicial proceeding, whether by written or spoken words or by conduct;

N. "total return trust" means a trust that is converted to a total return trust pursuant to Section 46-3A-105 NMSA 1978 or a trust the terms of which manifest the settlor's intent that the trustee will administer the trust in accordance with Section 46-3A-106 NMSA 1978; and

O. "trustee" includes an original, additional or successor trustee, whether or not appointed or confirmed by a court."

2001, Chapter 113, Section 104) is amended to read:

"46-3A-104. TRUSTEE'S POWER TO ADJUST.--

(a) A trustee may adjust between principal and income to the extent the trustee considers necessary if the trustee invests and manages trust assets as a prudent investor, the terms of the trust describe the amount that may or must be distributed to a beneficiary by referring to the trust's income, and the trustee determines, after applying the rules in Subsection (a) of Section 46-3A-103 NMSA 1978, that the trustee is unable to comply with Subsection (b) of Section 46-3A-103 NMSA 1978.

(b) In deciding whether and to what extent to exercise the power conferred by Subsection (a) of this section, a trustee shall consider all factors relevant to the trust and its beneficiaries, including the following factors to the extent they are relevant:

- (1) the nature, purpose and expected duration of the trust;
- (2) the intent of the settlor;
- (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 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 the Uniform Principal and Income 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) whether and to what extent the terms of the trust give the trustee the power to invade principal or accumulate income or prohibit the trustee from invading principal or accumulating income, and the extent to which the trustee has exercised a power from time to time to invade principal or accumulate income;

(8) the actual and anticipated effect of economic conditions on principal and income and effects of inflation and deflation; and

(9) the anticipated tax consequences of an adjustment.

(c) A trustee may not make an adjustment:

(1) that diminishes the income interest in a trust that requires all of the income to be paid at least annually to a surviving spouse and for which an estate tax or gift tax marital deduction would be allowed, in whole or in

part, if the trustee did not have the power to make the adjustment;

(2) that reduces the actuarial value of the income interest in a trust to which a person transfers property with the intent to qualify for a gift tax exclusion;

(3) that changes the amount payable to a beneficiary as a fixed annuity or a fixed fraction of the value of the trust assets;

(4) from any amount that is permanently set aside for charitable purposes under a will or the terms of a trust unless both income and principal are so set aside;

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

(6) if possessing or exercising the power to make an adjustment causes all or part of the trust assets to be included for estate tax purposes in the estate of an individual who has the power to remove a trustee or appoint a trustee, or both, and the assets would not be included in the estate of the individual if the trustee did not possess the power to make an adjustment;

(7) if the trustee is a beneficiary of the trust;

(8) if the trustee is not a beneficiary, but the adjustment would benefit the trustee directly or indirectly; or

(9) if the trust is a total return trust.

(d) If Paragraph (5), (6), (7) or (8) of Subsection (c) of this section applies to a trustee and there is more than one trustee, a co-trustee to whom the provision does not apply may make the adjustment unless the exercise of the power by the remaining trustee or trustees is not permitted by the terms of the trust.

(e) A trustee may release the entire power conferred by Subsection (a) of this section or may release only the power to adjust from income to principal or the power to adjust from principal to income if the trustee is uncertain about whether possessing or exercising the power will cause a result described in Paragraphs (1) through (6) or Paragraph (8) of Subsection (c) of this section or if 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 (c) of this section. The release may be permanent or for a specified period, including a period measured by the life of an individual.

(f) Terms of a trust that limit the power of a trustee to make an adjustment between principal and income do not affect the application of this section unless it is clear

from the terms of the trust that the terms are intended to deny the trustee the power of adjustment conferred by Subsection (a) of this section."

Section 3. A new section of the Uniform Principal and Income Act, Section 46-3A-105 NMSA 1978, is enacted to read:

"46-3A-105. CONVERSION TO TOTAL RETURN TRUST.--

A. Unless expressly prohibited by the governing instrument, a trustee may release the power to adjust as provided in Section 46-3A-104 NMSA 1978 or convert a trust to a total return trust as provided in this section if all of the following apply:

(1) the trust describes the amount that may or must be distributed to a beneficiary by referring to the trust's income and the trustee determines that conversion to a total return trust will enable the trustee to better carry out the purposes of the trust;

(2) the trustee provides a written notice of the trustee's decision to convert the trust to a total return trust specifying a prospective effective date for the conversion that may not be sooner than sixty days after the notice is provided to the qualified beneficiaries, determined as of the date the notice is provided and assuming nonexercise of all powers of appointment;

(3) there are one or more legally competent beneficiaries as provided in Paragraph (1) of Subsection K of

Section 46-3A-102 NMSA 1978 and one or more legally competent remainder beneficiaries described in either Paragraph (1) or (2) of Subsection K of Section 46-3A-102 NMSA 1978, determined as of the date the notice is provided; and

(4) no beneficiary has objected in writing to the conversion to a total return trust and noticed the objection to the trustee within sixty days after the notice was provided.

B. Conversion to a total return trust or reconversion to an income trust may be made by agreement between the trustee and all qualified beneficiaries of the trust. The trustee and all qualified beneficiaries may also agree to modify the distribution percentage, except that the trustee and the qualified beneficiaries may not agree to a distribution percentage less than three percent or greater than five percent.

C. The trustee may elect to petition the court to order conversion to a total return trust, including the reason that conversion under Subsection A of this section is unavailable because:

(1) a beneficiary timely objects to the conversion to a total return trust;

(2) there are no legally competent beneficiaries described in Paragraph (1) of Subsection K of Section 46-3A-102 NMSA 1978; or

(3) there are no legally competent beneficiaries described in Paragraph (1) or (2) of Subsection K of Section 46-3A-102 NMSA 1978.

D. A beneficiary may request the trustee to convert to a total return trust or adjust the distribution percentage pursuant to this section. If the trustee declines or fails to act within six months after receiving a written request from a beneficiary to do so, the beneficiary may petition the court to order the conversion or adjustment.

E. The trustee may petition the court prospectively to reconvert from a total return trust or to adjust the distribution percentage if the trustee determines that the reconversion or adjustment will enable the trustee to better carry out the purposes of the trust. A beneficiary may request the trustee to petition the court prospectively to reconvert from a total return trust or adjust the distribution percentage. If the trustee declines or fails to act within six months after receiving a written request from a beneficiary to do so, the beneficiary may petition the court to order the reconversion or adjustment.

F. In a judicial proceeding instituted under this section, the trustee may present information concerning:

(1) the trustee's support for, or opposition to, a conversion to a total return trust, a reconversion from a total return trust or an adjustment of the distribution

percentage of a total return trust, including whether the trustee believes conversion, reconversion or adjustment of the distribution percentage would enable the trustee to better carry out the purposes of the trust; and

(2) any other matter relevant to the proposed conversion, reconversion or adjustment of the distribution percentage.

G. A trustee's actions undertaken in accordance with this section shall not be determined improper or inconsistent with the trustee's duty of impartiality unless the court finds from all the evidence that the trustee acted in bad faith.

H. The court may order conversion to a total return trust, reconversion prospectively from a total return trust or adjustment of the distribution percentage of a total return trust if the court determines that the conversion, reconversion or adjustment of the distribution percentage will enable the trustee to better carry out the purposes of the trust.

I. If a conversion to a total return trust is made pursuant to a court order, the trustee may reconvert the trust to an income trust only:

(1) pursuant to a subsequent court order; or

(2) by filing with the court an agreement

made pursuant to Subsection B of this section to reconvert to

an income trust.

J. Upon a reconversion, the power to adjust, as described in Section 46-3A-104 NMSA 1978 and as it existed before the conversion, shall be revived.

K. An action may be taken under this section no more frequently than every three years, unless the court for good cause orders otherwise."

Section 4. A new section of the Uniform Principal and Income Act, Section 46-3A-106 NMSA 1978, is enacted to read:

"46-3A-106. ADMINISTRATION OF TOTAL RETURN TRUST.--

A. During the period that a trust is a total return trust, the trustee shall administer the trust in accordance with the provisions of this section unless otherwise expressly provided by the terms of the trust.

B. The trustee shall invest the trust assets seeking a total return without regard to whether the return is from income or appreciation of principal.

C. The trustee shall make income distributions in accordance with the governing instrument subject to the provisions of this section.

D. The distribution percentage for any trust converted to a total return trust by a trustee in accordance with Subsection A of Section 46-3A-105 NMSA 1978 shall be four percent, unless a different percentage has been determined in an agreement made pursuant to Subsection B of Section

46-3A-105 NMSA 1978 or ordered by the court pursuant to Subsection C of Section 46-3A-105 NMSA 1978.

E. The trustee shall pay to a beneficiary in the case of an underpayment within a reasonable time, and shall recover from a beneficiary in the case of an overpayment, either by repayment by the beneficiary or by withholding from future distributions to the beneficiary:

(1) an amount equal to the difference between the amount properly payable and the amount actually paid; and

(2) interest compounded annually at a rate per annum equal to the distribution percentage in the year or years during which the underpayment or overpayment occurs; provided that accrual of interest may not commence until the beginning of the trust year following the year in which the underpayment or overpayment occurs.

F. As used in Sections 46-3A-105 through 46-3A-113 NMSA 1978:

(1) "income" as the term appears in the governing instrument means the distribution amount;

(2) "distribution amount" means the annual amount equal to the distribution percentage multiplied by the average net fair market value of the trust's assets; and

(3) "average net fair market value of the trust's assets" means the net fair market value of the trust's

assets averaged over the lesser of the three preceding years or the period during which the trust has been in existence."

Section 5. A new section of the Uniform Principal and Income Act, Section 46-3A-107 NMSA 1978, is enacted to read:

"46-3A-107. DETERMINATION OF MATTERS IN ADMINISTRATION.--

A. The trustee may determine any of the following matters in administering a total return trust as the trustee deems necessary or helpful for the proper functioning of the trust:

(1) the effective date of a conversion to a total return trust pursuant to Section 46-3A-105 NMSA 1978;

(2) the manner of prorating the distribution amount for a short year in which a beneficiary's interest commences or ceases, or, if the trust is a total return trust for only part of the year, the trustee may elect to treat the trust year as two separate years, the first of which ends at the close of the day on which the conversion or reconversion occurs, and the second of which ends at the close of the trust year;

(3) whether distributions are made in cash or in-kind;

(4) the manner of adjusting valuations and calculations of the distribution amount to account for other payments from, or contributions to, the trust;

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

(6) which valuation dates to use and how many valuation dates to use; and

(7) valuation decisions concerning any asset for which there is no readily available market value, including:

(a) how frequently to value the asset;

(b) whether and how often to engage a professional appraiser to value the asset; and

(c) whether to exclude the value of the asset from the net fair market value of the trust's assets for purposes of determining the distribution amount.

B. For purposes of this section, any asset excluded pursuant to Subparagraph (c) of Paragraph (7) of Subsection A of this section shall be referred to as an "excluded asset" and the trustee shall distribute any net income received from the excluded asset as provided for in the governing instrument, subject to the following principles:

(1) the trustee shall treat each asset for which there is no readily available market value as an excluded asset unless the trustee determines that there are compelling reasons not to do so and the trustee considers all relevant factors, including the best interests of the beneficiaries;

(2) if tangible personal property or real property is possessed or occupied by a beneficiary, the trustee may not limit or restrict any right of the beneficiary to use the property in accordance with the governing instrument regardless of whether the trustee treats the property as an excluded asset;

(3) assets for which there is a readily available market value include cash and cash equivalents; stocks, bonds and other securities and instruments for which there is an established market on a stock exchange, in an over-the-counter market or otherwise; and any other property that can reasonably be expected to be sold within one week of the decision to sell without extraordinary efforts by the seller;

(4) assets for which there is no readily available market value include stocks, bonds and other securities and instruments for which there is no established market on a stock exchange, in an over-the-counter market or otherwise; real property; tangible personal property; and artwork and other collectibles."

Section 6. A new section of the Uniform Principal and Income Act, Section 46-3A-108 NMSA 1978, is enacted to read:

"46-3A-108. DISTRIBUTION OF TOTAL RETURN TRUST.--

A. Expenses, taxes and other charges that would otherwise be deducted from income if the trust was not a total

return trust may not be deducted from the distribution amount.

B. Unless otherwise provided by the governing instrument, the distribution amount each year shall be deemed to be paid from the following sources for that year in the following order:

- (1) net income determined as if the trust were not a total return trust;
- (2) other ordinary income as determined for federal income tax purposes;
- (3) net realized short-term capital gains as determined for federal income tax purposes;
- (4) net realized long-term capital gains as determined for federal income tax purposes;
- (5) trust principal comprising assets for which there is a readily available market value; and
- (6) other trust principal."

Section 7. A new section of the Uniform Principal and Income Act, Section 46-3A-109 NMSA 1978, is enacted to read:

"46-3A-109. RESTRICTIONS ON DISTRIBUTIONS.--

A. The distribution amount may not be less than the net income of the trust, determined without regard to the provisions of Sections 46-3A-105 through 46-3A-113 NMSA 1978, for a trust that was exempt, in whole or in part, from generation-skipping transfer tax on July 1, 2005 by reason of any effective date or transition rule.

B. Conversion to a total return trust shall not affect any provisions in the governing instrument:

(1) that directs or authorizes the trustee to distribute principal;

(2) that directs or authorizes the trustee to distribute a fixed annuity or a fixed fraction of the value of trust assets;

(3) that authorizes a beneficiary to withdraw a portion or all of the principal; or

(4) that in any manner diminishes an amount permanently set aside for charitable purposes under the governing instrument unless both income and principal are set aside."

Section 8. A new section of the Uniform Principal and Income Act, Section 46-3A-110 NMSA 1978, is enacted to read:

"46-3A-110. LIMITATIONS ON CONVERSION.--If a trustee is also a beneficiary of the trust and conversion or failure to convert would enhance or diminish the beneficial interest of that trustee, or if possession or exercise of the conversion power by a particular trustee alone would cause any individual to be treated as owner of a part of the trust for federal income tax purposes or cause a part of the trust to be included in the gross estate of any individual for federal estate tax purposes, then that trustee may not participate as a trustee in the exercise of the conversion power, except

that:

A. the trustee may petition the court under Subsection C of Section 46-3A-105 NMSA 1978 to order conversion in accordance with this section; and

B. a co-trustee or co-trustees to whom this section does not apply may convert the trust to a total return trust in accordance with Sections 46-3A-105 and 46-3A-106 NMSA 1978."

Section 9. A new section of the Uniform Principal and Income Act, Section 46-3A-111 NMSA 1978, is enacted to read:

"46-3A-111. RELEASE.--A trustee may irrevocably release the power granted by the provisions of Sections 46-3A-105 through 46-3A-113 NMSA 1978 if the trustee reasonably believes the release is in the best interests of the trust and its beneficiaries. The release may be personal to the releasing trustee or it may apply generally to some or all subsequent trustees. The release may be for any specified period, including a period measured by the life of an individual."

Section 10. A new section of the Uniform Principal and Income Act, Section 46-3A-112 NMSA 1978, is enacted to read:

"46-3A-112. REMEDIES.--

A. A trustee who reasonably and in good faith takes any action or omits to take any action pursuant to Sections 46-3A-105 through 46-3A-113 NMSA 1978 is not liable to any person interested in the trust.

B. If a trustee reasonably and in good faith takes or omits to take any action pursuant to Sections 46-3A-105 through 46-3A-113 NMSA 1978 and a person interested in the trust opposes the act or omission, in addition to any other remedy otherwise provided or available by law, the person may seek an order of the court directing the trustee to:

- (1) convert the trust to a total return trust;
- (2) reconvert from a total return trust;
- (3) change the distribution percentage; or
- (4) order any administrative procedures the court determines are necessary or helpful for the proper functioning of the trust.

C. A claim for relief pursuant to Subsection B of this section that is not barred by adjudication, consent or limitation is nevertheless barred as to any beneficiary who has received a written notice fully disclosing the matter unless a proceeding to assert the claim is commenced within six months after receipt of the statement."

Section 11. A new section of the Uniform Principal and Income Act, Section 46-3A-113 NMSA 1978, is enacted to read:

"46-3A-113. APPLICABILITY.--

A. Sections 46-3A-105 through 46-3A-113 NMSA 1978 shall apply to trusts in existence on July 1, 2005 and to trusts created on or after that date.

B. Sections 46-3A-105 through 46-3A-113 NMSA 1978 shall be construed to apply to the administration of a trust that is administered in New Mexico under New Mexico law or that is governed by New Mexico law with respect to the meaning and effect of its terms unless:

(1) the trust is a trust described in Section 170(f)(2)(B), 664(d), 2702(a)(3) or 2702(b) of the federal Internal Revenue Code of 1986;

(2) the governing instrument expressly prohibits the use of Sections 46-3A-105 through 46-3A-113 NMSA 1978 by specific reference to one or more provisions of those sections; or

(3) the terms of a trust in existence on July 1, 2005 incorporate provisions that operate as a total return trust. The trustee or a beneficiary of such a trust may adopt provisions in Sections 46-3A-105 through 46-3A-113 NMSA 1978 that do not contradict provisions in the governing instrument."

Section 12. EFFECTIVE DATE.--The effective date of the provisions of this act is July 1, 2005. _____