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BILL ANALYSIS

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Senate Bill 1051 (as enrolled) **PUBLIC ACT 314 of 2004**
Sponsor: Senator Alan L. Cropsey
Senate Committee: Judiciary
House Committee: Judiciary

Date Completed: 9-1-04

RATIONALE

The Estates and Protected Individuals Code (EPIC) was enacted in 1998 to replace Michigan's Revised Probate Code, which had been enacted 20 years earlier. While the older statute had primarily addressed the settlement of decedents' estates, EPIC also governs the administration of trusts and the powers of trustees, and includes a prudent investor rule for fiduciaries. The recent legislation also repealed and recodified several other statutes, including the Disclaimer of Property Interests Act. These changes were the culmination of about 10 years of review by the Council of the Probate and Estate Planning Section of the State Bar, including six years of preparation by probate lawyers and judges, probate registers, and corporate trust officers. Since EPIC was enacted, the Council has continued to review the law. The Council found a number of ambiguities in EPIC, and raised concerns about provisions dealing with trustees' disclosure of information to beneficiaries.

CONTENT

The bill amended provisions of the Estates and Protected Individuals Code that pertain to trusts and estates. Among other things, the bill does the following:

-- **Revises the information that a trustee must give to beneficiaries in a statement of account.**
-- **Provides that a beneficiary's claim for breach of trust will be barred one year after he or she is sent a report disclosing the existence of a potential claim, rather than an annual or final account; and provides for a five-year statute of limitations in other cases.**
-- **Requires the repayment of improper distributions from a trust.**
-- **Requires the payment of interest on money that a fiduciary deposited with a county treasurer, when the money is paid to a claimant.**
-- **Provides that a child is born in wedlock, for purposes of intestate succession, if the child is not conceived or born during a marriage, but his or her parents marry after the child's conception or birth.**
-- **Excludes the value of property in trust for the benefit of a child of a decedent, from the intestate share of a surviving spouse who married the decedent after he or she made a will.**
-- **Revises provisions for the disclaimer of a property interest.**
-- **Expands the authority of a personal representative to make certain decisions regarding taxation.**

The bill took effect on September 1, 2004.

<u>Trust Administration</u>

<u>Statement of Account</u>. Under EPIC, a trustee must provide a statement of account to each current trust beneficiary at least annually and on termination of the trust or a change of the trustee. Upon reasonable request, a trustee also must provide a statement of account to each interested trust beneficiary who is not a current trust beneficiary.

The bill specifies that a statement of account is a report by the trustee that, at a minimum, must list the trust assets, giving their market values if feasible, the trust liabilities, receipts, and disbursements, and state the source and amount of the trustee's compensation. A particular format or formality is not required for a report or statement of account unless a court specifies its content and manner of presentation.

Claim for Breach of Trust. Previously, a beneficiary's claim against a trustee for breach of trust was barred unless a proceeding on the claim was begun within one year after the beneficiary received an annual or final account (unless the claim had been previously barred by adjudication, consent, or limitation). An account had to contain certain information described in EPIC, including sufficient information to put interested persons on notice as to all significant transactions affecting administration during the accounting period, and significant transactions that did not affect the amount for which the trustee was accountable. An account had to be provided as required for notice of a hearing. The bill deleted all of these provisions.

Under the bill, a beneficiary is barred from commencing a proceeding against a trustee for breach of trust if the proceeding is not begun within one year after the date the beneficiary or a representative of the beneficiary is sent a report that adequately discloses the existence of a potential claim for breach of trust, and informs the beneficiary of the time allowed for commencing a proceeding. A beneficiary also may be barred from commencing a proceeding by adjudication, consent, ratification, estoppel, or other limitation.

Under the bill, a report adequately discloses the existence of a potential claim for breach of trust if it provides sufficient information so that the beneficiary or representative knows of the potential claim or should have inquired into its existence.

If the one-year period of limitations does not apply, a proceeding against a trustee for breach of trust must be commenced within five years of the first of the following to occur:

-- The trustee is removed, resigned, or died.
-- The beneficiary's interest in the trust terminates.
-- The trust terminates.

Multiple Trustees. Under the bill, if there are two or more trustees and the trust instrument expressly provides for the execution of any of their powers by both or all of them, the provisions of the trust instrument govern. Previously, this applied if there were more than two, rather than two or more, trustees.

Tax Matters. The Code authorizes a trustee to take certain actions in connection with a tax matter. These include making, revising, or revoking an available allocation, consent, or election affecting a tax that is appropriate to carry out the settlor's estate planning objectives and to reduce the overall burden of taxation. After making this decision, the trustee may make compensating adjustments between principal and income. Under the bill, the trustee may make these compensating adjustments in the manner provided by the Uniform Principal and Interest Act.

Repayment of Improper Distribution. Under the bill, unless a distribution or payment may no longer be questioned because of adjudication, estoppel, or other limitation, a distributee or claimant who receives property that is improperly distributed or paid from a trust must return the property and any income and gain from it since distribution, if the recipient has the property. If not, the recipient must pay the value of the property as of the date of distribution or payment and any income or gain from the property since distribution.

Payment by County Treasurer

The Code requires a fiduciary making final distribution to deposit with the county treasurer money or personal property that belongs to an heir, devisee, trust beneficiary, or claimant whom the fiduciary cannot locate or who declines to accept the money, or money or property belonging to a person whose right is the subject of appeal from a court order.

A person entitled to money deposited with a county treasurer may petition the court for an order directing the treasurer to pay over the money. If satisfactory proof of the claimant's right to the money is made, the court must order the county treasurer to pay the money to the claimant. Under the bill, the court must order the treasurer to pay the money and interest earned on it, less the treasurer's fee, to the claimant.

The Code provides that, if a person who cannot be located or who declined to accept the money does not claim it within three years after the money has been deposited with the county treasurer, the money that would have been distributed to that person, less expenses, must be distributed by court order to everyone who would be entitled to it if the person had died, and his or her claim is forever barred. Under the bill, interest earned on the money also must be distributed.

The bill deleted provisions requiring a county treasurer, at the beginning of his or her term of office, to give a bond running to the judge, with two or more sureties approved by the court, subject to conditions specified in the Code. The bill also deleted a provision under which the court could require the county treasurer, at any time, to give a new or additional bond.

Child Born in Wedlock

The Code states that, for purposes of intestate succession (inheritance in the absence of a will) by, through, or from an person, an individual is the child of his or her natural parents, regardless of their marital status. The Code describes ways in which the parent and child relationship may be established.

The bill specifies that a child who is not conceived or born during a marriage is an individual born in wedlock if the child's parents marry after the conception or birth of the child.

Surviving Spouse's Intestate Share

Under EPIC, if the surviving spouse of a decedent had married that person after he or she made a will, the surviving spouse is entitled to a share of the decedent's estate. The surviving spouse is entitled to the value of the share of the estate that he or she would have received if the decedent had died intestate (without a will), subject to certain exclusions. The exclusions apply to property that was left to a child of the decedent who was born before he or she married the surviving spouse and who is not the surviving spouse's child, and property devised to a descendant of the child. Under the bill, these exclusions also apply to property in trust for the benefit of such a child or his or her descendant.

Disclaimer of Interest

Part 9 of Article 2 is known as the "Disclaimer of Property Interests Law", and provides for the right of a person to disclaim, or give up, a disclaimable interest in property. ("Disclaimable interest" includes property, the right to receive or control property, and a power of appointment.) A disclaimer may be of a fractional or percentage share, or a limited interest or estate. Under the bill, a person also may disclaim a specific asset, an interest in a specific asset, or a pecuniary amount.

Previously, except for a trust or a power of attorney, EPIC stated that the right to disclaim existed notwithstanding a spendthrift provision or a restriction or limitation on the right to disclaim contained in the governing instrument (a deed, will, contract, etc. under which property devolves, a property right is created, or a contract right is created). The bill provides, instead, that unless the governing instrument is a trust instrument that does not authorize the trustee to disclaim, or a power of attorney that denies the agent (the person acting under the power of attorney) the authority to disclaim, the right to disclaim exists notwithstanding either of the following:

-- A spendthrift provision or similar restriction that limits the interest of the disclaimant.
-- A restriction or limitation on the right to disclaim contained in the governing instrument.

Previously, a spouse who was the beneficiary of a property interest for which a marital deduction was claimed under the Internal Revenue Code, could not disclaim his or her interest later than nine months after the date on which the governing instrument containing the transfer was irrevocable. The bill deleted that provision.

Personal Representative: Tax Elections

A personal representative is a person responsible for administering an estate and winding up its affairs. The Code authorizes a personal representative to take certain actions for the benefit of interested persons. Under the bill these include making, revising, or revoking an available allocation, consent, or election in connection with a tax matter as appropriate to carry out the decedent's estate planning objectives and reduce the overall burden of taxation. (Previously, a personal representative could make tax elections appropriate to carry out the decedent's estate planning objectives and to reduce the overall burden of taxation.)

Under the Code, the authority to make elections includes electing to take expenses as estate tax or income tax deductions; electing to allocate the exemption from the tax on generation skipping transfers among transfers subject to estate or gift tax; and electing to have all or part of a transfer for a spouse's benefit qualify for the marital deduction. The authority under the bill also includes the following for Federal estate tax purposes:

-- Electing the date of death or an alternate valuation date.
-- Excluding or including property from the gross estate.
-- Valuing property.

In addition, under the bill, the personal representative's authority includes joining with the surviving spouse or his or her personal representative in the execution and filing of a joint income tax return and consenting to a gift tax return filed by the surviving spouse or his or her personal representative.

Claims against an Estate: Time Limit

Under EPIC, a claim against a decedent's estate that arose before the decedent's death is barred against the estate, the personal representative, the decedent's heirs and devisees, and nonprobate transferees of the decedent, unless the claim is presented within time limits specified in the Code. The time limit is three years after the decedent's death if the personal representative did not publish notice to creditors to present their claims, as required in Section 3801. Under the bill, this time limit also applies if a trustee did not publish notice as required in Section 7504 (which requires a trustee to publish notice if there is no personal representative).

Apportionment

The Code prescribes the manner of apportioning an estate, inheritance, or other death tax assessed under the laws of this or another state, political subdivision, or country. The Code also provides for the apportionment of a credit given under the U.S. estate tax laws for a tax paid to another country or a political subdivision. These provisions include the apportionment of interest and penalties.

The bill authorizes the probate court to direct apportionment in the manner it considers equitable, if the court finds that it is inequitable to apportion taxes, credits, interest, and penalties as prescribed in EPIC. (Previously, the court could equitably apportion only interest and penalties.)

The Code's formula for apportioning taxes provides for the apportionment of tax liability remaining after the application of certain provisions, including a tax imposed with respect to property passing by survivorship or intestacy. Under the bill, this also applies to a tax imposed with respect to property passing by beneficiary designation.

Other Provisions

The bill amended EPIC's definition of "interested person" or "person interested in an estate" to include the incumbent fiduciary. As before, the term also includes, among others, an heir, devisee, child, spouse, creditor, and beneficiary, and any other person who has a property right in or claim against a trust estate or the estate of a decedent, ward, or protected individual. (An interested person is entitled to receive various notices under EPIC.)

The Code provides that a future interest under the terms of a trust is contingent on the beneficiary's surviving the distribution date. (That is, if a person will become entitled to a benefit under a trust in the future, he or she must survive until the time the future interest takes effect.) Under the bill, this does not apply to a future interest if the beneficiary died or irrevocably transferred the interest before April 1, 2000 (the date EPIC took effect).

MCL 700.1105 et al.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

Rather than waiting another 20 years to overhaul EPIC, this legislation continues the process of keeping the law up to date and workable for practitioners, while protecting the interests of individuals. For the most part, the amendments resolve ambiguities and internal inconsistencies within the law. For example, requiring the repayment of improper distributions from a trust is consistent with existing requirements regarding the administration of a decedent's estate. Explicitly including an incumbent fiduciary as an interested person is necessary because a fiduciary does not have a property right in or a claim against an estate, and some courts therefore have not viewed a fiduciary as an interested person.

The bill also confirms the requirement that interest earned on unclaimed property deposited with a county treasurer be distributed to the claimant, and relieves county treasurers of having to post a bond.

The bill makes it clear in EPIC that a child is born in wedlock if his or her parents marry after the child's conception or birth. Evidently, this always has been the law in Michigan, but it was not stated in statute.

In addition, the bill contains various other "cleanup" amendments. Previously, in order to preserve the Federal estate tax marital deduction, it was considered necessary to set a time limit on a spouse's disclaimer of a property interest for which a marital deduction was claimed. Since this is not the case, the bill deleted that language. The bill also authorizes the probate court to apportion taxes and credits equitably. Apparently, this language was inadvertently omitted when EPIC was drafted.

Supporting Argument

Section 7307 of EPIC had explicitly described the required contents of a trustee's account, in order for it to be sufficient to bar claims more than one year after the account had been delivered. According to the Council of the Probate and Estate Planning Section, this provision proved to be unworkable for almost all trustees, and the amendment moves to a concept embodied in the Uniform Trust Code. Under the bill, a trustee's report will be adequate to bar claims after a one-year period if it supplies information sufficient to disclose the existence of a possible claim and informs the beneficiary of the period for making a claim. If sufficient information is not supplied, the time limit for making a claim will be five years after certain events.

Section 7303(3) prescribes a trustee's obligation to supply information to trust beneficiaries, and refers to a statement of account in a number of places. Since the amendment to Section 7307 shifts from language describing an account to the term "report", the revisions to Section 7303(3) bring that section into harmony with Section 7307 and reflect the Uniform Trust Code concept of a report, according to the Council. As the Council pointed out, a trustee's report might include information other than simple accounting information. For example, if a trustee invests in securities of an investment trust to which the trustee provides services in a capacity other than a trustee, the trustee may disclose in its statement of account that it is compensated for those services by the investment trust out of fees charged to the trust. "Disclosure should be deemed complete if the persons entitled to receive a copy of the trustee's statement of account are informed of such charges and the account notifies those persons of the availability of a report…which discloses the rate and method by which the compensation for services is determined."

Legislative Analyst: Suzanne Lowe

FISCAL IMPACT

To the extent that it affects the number of disputes over wills and trusts, the bill will have an indeterminate fiscal impact on the judiciary.

Also, to the extent that counties previously benefited from any interest earned on deposits they hold before the funds are claimed, the bill will have a negative fiscal impact on local government by requiring county treasurers to pay interest to claimants.

Fiscal Analyst: Bethany Wicksall

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.