

No. 1998-141

AN ACT

SB 1205

Amending Titles 15 (Corporations and Unincorporated Associations) and 20 (Decedents, Estates and Fiduciaries) of the Pennsylvania Consolidated Statutes, further providing for investment of trust funds, for transfer of trust or other assets to institutional trustee and for establishment or use of common trust funds authorized; imposing limits on the exercise of certain trustee powers and the ability of beneficiaries to appoint trustees under certain circumstances; and making editorial changes.

The General Assembly of the Commonwealth of Pennsylvania hereby enacts as follows:

Section 1. Sections 5548(b), (c) and (e), 5549(c) and 5585(a) of Title 15 of the Pennsylvania Consolidated Statutes are amended to read:

§ 5548. Investment of trust funds.

* * *

(b) Use and management.—Except as otherwise permitted under [the Estates Act of 1947] 20 Pa.C.S. Ch. 61 (relating to estates), the board of directors or other body shall apply all assets thus received to the purposes specified in the trust instrument. The directors or other body shall keep accurate accounts of all trust funds, separate and apart from the accounts of other assets of the corporation.

(c) Determination of income.—

(1) With respect to any assets thus received (including any participation in any common trust fund) so much of the net realized capital gains as of the end of any fiscal year of the corporation as the directors or other body shall, within four months after the end of such year, in their sole discretion, allocate to income for such fiscal year shall be deemed income.

(2) The amount allocated under paragraph (1) of this subsection, when added to all other income derived by the corporation from the same assets or participation in a common trust fund for such fiscal year, shall not exceed 9% of the market value (as of the end of such fiscal year) of the principal remaining with respect to such assets or participation after allocation of such gain to income.

(3) Allocation to income of realized capital gains in a common trust fund may be made in accordance with the provisions of paragraphs (1) and (2) of this subsection without regard to whether the capital gains in question were realized before or after any particular trust or fund became a part of such common trust fund and without regard to whether the separate records maintained with

respect to such particular trust or fund reflect the existence of a capital gain in such trust or fund.]

(1) Unless otherwise specifically directed in the trust instrument, the board of directors or other body may elect to be governed by this subsection with respect to assets thus received, including any participation in any common trust fund.

(2) To make an election under this subsection, the board of directors or other body shall adopt and follow an investment policy seeking a total return for the assets held by the corporation or in the name of a nominee of the corporation or by an institutional trustee pursuant to section 5549 (relating to transfer of trust or other assets to institutional trustee), whether the return is to be derived from capital appreciation, earnings or distributions with respect to the capital or both. The policy constituting the election shall be in writing, shall be maintained as part of the permanent records of the corporation and shall recite that it constitutes an election to be governed by this subsection.

(3) If an election is made to be governed by this subsection, the term "income" shall mean a percentage of the value of the assets so held by or for the corporation. The board of directors or other body shall in a writing maintained as part of the permanent records of the corporation annually select a percentage and determine that it is consistent with the long-term preservation of the real value of the assets, but in no event shall the percentage be less than 2% nor more than 7% per year.

(4) The board of directors or other body may revoke an election to be governed by this subsection if the revocation is made as part of an alternative investment policy seeking the long-term preservation of the real value of the assets thus received. The revocation and alternative investment policy shall be in writing and maintained as part of the permanent records of the corporation.

(5) For purposes of applying this subsection, the value of the assets of the corporation shall be the fair market value of the assets so held by or for the corporation, determined at least annually and averaged over a period of three or more preceding years. However, if the assets have been held for less than three years, the average shall be determined over the period during which the assets have been held.

* * *

[(e) Definition.—As used in subsection (c) of this section "net realized capital gains as of the end of any fiscal year" means the balance accumulated as of such date, since the inception of the trust or fund or common trust fund, as the case may be, of all realized gains less realized losses, computed in the manner provided in sections 1001 et seq. of the Internal Revenue Code of 1954 on the basis of actual cost, or in the case of property transferred to the fund or trust, on the basis of fair market value on the date of transfer.]

§ 5549. Transfer of trust or other assets to institutional trustee.

* * *

(c) Amount and frequency of payment.—Such corporate trustee shall pay, at least semi-annually or at more frequent intervals if so agreed, the net income from such assets, which *income* may [~~include so much of the realized appreciation of principal as the board of directors or other body of the corporation may deem prudent~~] *be determined under section 5548(c) (relating to investment of trust funds) if such election is properly made by the board of directors or other body of the corporation*, to the corporation for use and application to the purpose or purposes for which the assets were received by the corporation.

§ 5585. Establishment or use of common trust funds authorized.

(a) General rule.—Every nonprofit corporation may establish and maintain one or more common trust funds, the assets of which shall be held, invested and reinvested by the corporation itself or by a corporate trustee to which the assets have been transferred pursuant to section 5549 (relating to transfer of trust or other assets to institutional trustee). Upon the payment by the corporate trustee to the nonprofit corporation of the net income from such assets, *which income may be determined under section 5548(c) (relating to investment of trust funds) if such election is properly made by the board of directors or other body of the corporation*, for use and application to the several participating interests in such common trust fund, the proportionate participation of each interest in such net income shall be designated by the corporate trustee. The nonprofit corporation may, at any time, withdraw the whole or part of any participating interest in such common trust fund for distribution by it as provided in this subchapter.

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Section 2. Title 20 is amended by adding a chapter to read:

CHAPTER 75
LIMITATIONS ON EXERCISE OF TRUSTEE POWERS
AND POWERS OF BENEFICIARIES TO APPOINT TRUSTEES

Sec.

- 7501. Legislative intent.
- 7502. Definitions.
- 7503. Application of chapter.
- 7504. Certain trustee powers not exercisable.
- 7505. Joint powers and appointment of nondisqualified substituted trustees.
- 7506. Certain powers of beneficiaries not exercisable.

§ 7501. Legislative intent.

This chapter is enacted to codify, clarify and confirm certain existing common law principles of fiduciary and trust law relating to conflicts of interest on the part of trustees.

§ 7502. Definitions.

The following words and phrases when used in this chapter shall have the meanings given to them in this section unless the context clearly indicates otherwise:

“Interested party.” Each trustee then serving and each person having an interest in income or principal whom it would be necessary to join as a party in a proceeding for the judicial settlement of a trustee’s account. The term “interested party” does not include a person who has not attained majority or is otherwise incapacitated unless a court has appointed a guardian for the person for some purpose other than acting under section 7503 (relating to application of chapter) or an agent has been appointed under a durable power of attorney that is sufficient to grant authority to act under section 7503.

§ 7503. Application of chapter.

(a) General rule.—This chapter shall apply to:

(1) Any trust created under a governing instrument executed on or after March 21, 1999, unless the governing instrument expressly provides that this chapter does not apply.

(2) Any trust created under a governing instrument executed before March 21, 1999, unless all interested parties affirmatively elect on or before December 21, 2001, by a written declaration signed by or on behalf of each interested party and delivered to the trustee, not to be subject to the application of this chapter. In the case of a testamentary trust, the declarations shall be filed with the register in the county in which the will was admitted to probate.

(b) Exclusion.—This chapter shall not apply to:

(1) Any trust during the time that the trust is revocable or amendable by its settlor.

(2) A spouse of a decedent or settlor where the spouse is the trustee of a testamentary or inter vivos trust for which a marital deduction has been allowed.

(3) A trustee who possesses in his individual capacity an unlimited right to withdraw the entire principal of the trust or has a general testamentary power of appointment over the entire principal of the trust.

(4) A trust under a governing instrument that by specific reference expressly rejects the application of this chapter.

(5) A trust created under a governing instrument executed on or before March 21, 1999, if no part of the principal of the trust would be included in the gross estate of the trustee for Federal estate tax purposes if the trustee had died on March 21, 1999, without having exercised the power under the governing instrument to make discretionary distributions of principal or income to or for the benefit of the trustee, the trustee’s estate or the creditors of either.

§ 7504. Certain trustee powers not exercisable.

(a) General rule.—The following powers conferred by a governing instrument upon a trustee in his or her capacity as a trustee shall not be exercised by that trustee:

(1) The power to make discretionary distributions of either principal or income to or for the benefit of the trustee, the trustee's estate or the creditors of either unless the power is either:

(i) limited by an ascertainable standard relating to the trustee's health, education, support or maintenance within the meaning of 26 U.S.C. §§ 2041 (relating to powers of appointment) and 2514 (relating to powers of appointment); or

(ii) exercisable by the trustee only in conjunction with another person having a substantial interest in the property subject to the power which is adverse to the interest of the trustee within the meaning of 26 U.S.C. § 2041(b)(1)(C)(ii).

(2) The power to make discretionary distributions of either principal or income to satisfy any of the trustee's personal legal obligations for support or other purposes.

(3) The power to make discretionary allocations in the trustee's personal favor of receipts or expenses as between income and principal unless the trustee has no power to enlarge or shift any beneficial interest except as an incidental consequence of the discharge of the trustee's fiduciary duties.

(4) The power to exercise any of the powers proscribed in this subsection with regard to an individual other than the trustee to the extent that the individual could exercise a similar prohibited power in connection with a trust that benefits the trustee.

(b) Limited exercise of prohibited power.—

(1) If a trustee is prohibited by subsection (a)(1) from exercising a power conferred upon the trustee, the trustee nevertheless may exercise that power but shall be limited to distributions for the trustee's health, education, support or maintenance to the extent otherwise permitted by the terms of the trust.

(2) Unless otherwise prohibited by the provisions of this section, a trustee may exercise a power described herein in favor of someone other than the trustee, the trustee's estate or the creditors of either.

§ 7505. Joint powers and appointment of nondisqualified substituted trustees.

If a governing instrument contains a power proscribed under section 7504 (relating to certain trustee powers not exercisable), the following shall apply:

(1) If the power is conferred on two or more trustees, it may be exercised by the trustee or trustees who are not so prohibited as if they were the only trustee or trustees.

(2) If there is no trustee in office who can exercise the power as provided in paragraph (1), the court, upon petition and hearing after such notice as it may direct, shall appoint a trustee who is not disqualified and

whose term in office shall be as the court directs for the sole purpose of exercising the powers that the other trustees cannot exercise.

§ 7506. Certain powers of beneficiaries not exercisable.

(a) General rule.—No beneficiary of a trust in an individual, trustee or other capacity may appoint or remove and appoint a trustee who is related or subordinate to the beneficiary within the meaning of 26 U.S.C. § 672(c) (relating to definitions and rules) unless:

(1) the trustee's discretionary power to make distributions to or for the beneficiary is limited by an ascertainable standard relating to the beneficiary's health, education, support or maintenance within the meaning of 26 U.S.C. §§ 2041 (relating to powers of appointment) and 2514 (relating to powers of appointment);

(2) the trustee's discretionary power may not be exercised to satisfy any of the beneficiary's legal obligations for support or other purposes; and

(3) the trustee's discretionary power may not be exercised to grant to the beneficiary a general power to appoint property of the trust to the beneficiary, the beneficiary's estate or the creditors thereof within the meaning of 26 U.S.C. § 2041.

(b) Exception.—This section shall not apply if the appointment of the trustee by the beneficiary may be made only in conjunction with another person having a substantial interest in the property of the trust subject to the power which is adverse to the exercise of the power in favor of the beneficiary within the meaning of 26 U.S.C. § 2041(b)(1)(C)(ii) or the appointment is in conformity with a procedure governing appointments approved by the court before December 21, 1998.

Section 3. Title 20 is amended by adding a section to read:

§ 8113. *Charitable trusts.*

(a) *Election.*—*Notwithstanding the foregoing provisions of this chapter, the trustee of a trust held exclusively for charitable purposes may elect to be governed by this section unless the governing instrument expressly provides that the election provided by this section shall not be available.*

(b) *Eligibility for election.*—*To make an election under this section, the trustee shall adopt and follow an investment policy seeking a total return for the investments held by the trust, whether the return is to be derived from appreciation of capital or earnings and distributions with respect to capital or both. The policy constituting the election shall be in writing, shall be maintained as part of the permanent records of the trust and shall recite that it constitutes an election to be governed by this section.*

(c) *Effect of election.*—*If an election is made to be governed by this section, the term "income" shall mean a percentage of the value of the trust. The trustee shall in a writing maintained as part of the permanent records of the trust annually select the percentage and determine that it is consistent with the long-term preservation of the real value of the principal of the trust, but in no event shall the percentage be less than 2% nor more*

than 7% per year. The term "principal" shall mean all other assets held by the trustee with respect to the trust.

(d) Revocation of election.—The trustee may revoke an election to be governed by this section if the revocation is made as part of an alternative investment policy seeking the long-term preservation of the real value of the principal of the trust. The revocation and alternative investment policy shall be in writing and maintained as part of the permanent records of the trust.

(e) Value determination.—For purposes of applying this section, the value of the trust shall be the fair market value of the cash and other assets held by the trustee with respect to the trust, whether such assets would be considered "income" or "principal" under the other provisions of this chapter, determined at least annually and averaged over a period of three or more preceding years. However, if the trust has been in existence less than three years, the average shall be determined over the period during which the trust has been in existence.

Section 4. The amendment or addition of the following provisions shall apply to all trusts, whether created before, on or after the effective date of this act:

- (1) 15 Pa.C.S. §§ 5548(b), (c) and (e), 5549(c) and 5585(a).
- (2) 20 Pa.C.S. § 8113.

Section 5. This act shall take effect immediately.

APPROVED—The 21st day of December, A.D. 1998.

THOMAS J. RIDGE