

## Memorandum Urging Approval

NYSBA #10-GOV

April 4, 2013

A. 1185

By: M or A Weinstein

S. 4952

By: Senator Bonacic

Assembly Committee: Judiciary

Senate Committee: Judiciary

Effective Date: 60 days after becoming law

AN ACT to amend the estates, powers and trusts law, in relation to the payment of interest on delayed legacies; and to repeal paragraphs (d) and (e) of section 11-1.5 of the estates, powers and trusts law and subdivision 7 of section 2102 of the surrogate's court procedure act relating thereto

### **THE NEW YORK STATE BAR ASSOCIATION SUPPORTS THIS LEGISLATION AND URGES GUBERNATORIAL APPROVAL**

This bill, developed by the Association's Trusts and Estates Law Section, would address three issues related to the current statutory scheme that deals with payment of interest on delayed legacies.

First, the bill would change the applicable interest rate on a delayed payment of a legacy from a statutorily fixed rate of 6% to a flexible interest rate tied to the federal funds rate. A legatee should be paid an interest rate that reflects the time value of money. The current interest rate was prevalent in 1985 when the statutory rate of 6% was put into effect, but it does not reflect current economic reality. Setting an interest rate at too high a rate punishes a residuary beneficiary whose share of the estate is diminished when an interest rate is paid to a legatee. Likewise, setting an interest at too low a rate hurts a legatee and enriches a residuary beneficiary.

If there is a delay in the payment of interest that is unreasonable, the Surrogate's court retains the power to charge the legal rate of interest to be paid by an errant fiduciary.

This bill would set the interest rate on the first business day of each calendar year for that calendar year at the federal funds rate less 1%, but in no event less than 1/2 of 1%. This rate reflects the interest rate actually earned by an estate on deposit accounts.

Next, the proposal would make the payment of interest mandatory. Currently, Surrogate's courts vary in their application of the current statute on a delayed payment of a legacy. Some courts require a formal demand on a fiduciary and then the commencement of a judicial proceeding. Other courts do not require a formal demand prior to the commencement of a proceeding. Some courts consider payment of interest in the discretion of the court and other courts deem it mandatory.

Under current law, unless an estate fiduciary agrees to pay the interest, a legatee has to institute a costly judicial proceeding to obtain the payment of interest. Thus, only legatees of large bequests will find it economically feasible to go through with the proceeding. By the same token, given the uncertainty in the law a fiduciary who agrees to pay interest absent a court proceeding risks a challenge from residuary beneficiaries for such payment.

Because the interest rate under this proposal would reflect what the estate is actually earning, the bill makes a legatee whose payment is delayed entitled to interest automatically seven months after a fiduciary in an estate is appointed.

Finally, the bill would revise tax treatment of paid interest in light of the Principal and Income Act. Under current income tax law, the legatee must report the interest as interest income, but the estate cannot deduct the interest as an expense. To be tax efficient, the interest paid on delayed payment of a legacy should be characterized under the New York Principal and Income Act (EPTL 11-A) as accounting income, so that its payment will carry out the distributable net income (“DNI”) in the same manner that the share of income due a pecuniary legacy in a trust carries out DNI.

In addition to the support of State Bar Association, this legislation is supported by the Office of Court Administration, the New York Bankers Association, and the New York City Bar Association.

Based on the foregoing, the State Bar Association supports the enactment of this legislation, which was developed by its Trusts and Estates Law Section, and urges Governor Cuomo’s **APPROVAL** of the bill.