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The Need for a New Type of Purpose Trust, the Stewardship Trust

*Susan N. Gary**

I. History of Purpose Trusts

The Uniform Trust Code (UTC) authorizes trusts for noncharitable purposes that lack an identifiable beneficiary. UTC Section 408 authorizes a trust for the care of an animal, and UTC Section 409 authorizes a trust for a noncharitable purpose without an ascertainable beneficiary. This latter type of trust is often called a purpose trust and that identifier will be used in this essay. Sections 408 and 409 built on the use of honorary trusts for noncharitable purposes, but create an actual trust structure, with certain constraints. A trust that meets the requirements of either section will be valid and enforceable.

A few creative lawyers are now using purpose trusts for business planning,[1] and Section 409 certainly permits doing so, but the structure and constraints of Section 409 are not well suited for trusts holding the assets of a business. Given the history of Sections 408 and 409, it seems likely that business trusts were not on the minds of the UTC Drafting Committee. The constraints built into these sections reflect concerns about the types of purpose trusts that had surfaced in cases and therefore were envisioned by the drafters. A trust used for business purposes has different needs, and the concerns related to such a trust are different. The addition of a new section to the UTC, authorizing a "stewardship trust," will address the needs and concerns of a trust holding the assets of business.

Under the common law a trust must have a beneficiary, but an exception has long existed for charitable trusts. Trusts that had neither an identifiable beneficiary nor a charitable purpose were invalid and unenforceable.[2] In some cases, courts refused to permit an intended trustee

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* Orlando J. and Marian H. Hollis Professor of Law, University of Oregon. A more thorough examination of steward-ownership, the history of purpose trusts, and the new Oregon stewardship trust statute can be found in *The Oregon Stewardship Trust: A New Type of Purpose Trust that Enables Steward-Ownership of a Business*, posted on SSRN at https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3426845.

1 *See* Alexander A. Bove, Jr., *The Purpose of Purpose Trusts*, 18 Prob. & Prop., May/June 2004, at 34, 37.

2 Restatement (Second) of Trusts § 123 (Am. Law Inst. 1959); Restatement (Third) of Trusts § 47 cmt. d (Am. Law Inst. 2003).

to carry out the trust, and the intended trust failed.[3] Over time, courts became more willing to authorize honorary trusts.[4] Both the Restatement (Second) and Restatement (Third) of Trusts provide that an intended trustee has the power, but not the duty, to carry out a trust for a purpose.[5] If the intended trustee were willing to carry out the terms, the trustee could do so, but no one could enforce the intended purposes. The intended trustee held the property as a resulting trust for the settlor's successors in interest, and if the intended trustee refused or failed to carry out the purposes, the property would be distributed through the settlor's estate, to heirs or beneficiaries. The Restatements provide for a 21-year limit on honorary purpose trusts, so that the trust will not violate the rule against perpetuities.[6] The Restatements also limit honorary trusts to those with purposes that are not capricious.[7]

In drafting Sections 408 and 409 the UTC drafters had in mind the types of trusts that courts had treated as honorary trusts.[8] The Restatements and the comments to the UTC cite cases in which courts had found honorary trusts when the purposes were for the care of animals, for a distribution of property for benevolent (but not charitable) purposes, or for care of a gravesite, the building of a memorial, or the saying of masses.[9] With these purposes in mind, the UTC drafters created a statute that would authorize trusts for these purposes, with certain restrictions to avoid the problems that otherwise accompanied noncharitable trusts without ascertainable beneficiaries.

Sections 408 and 409 both provide for enforcement by a person named by the settlor or by the court.[10] Both sections limit the time for enforcement to a fixed number of years, to avoid violation of the rule against perpetuities.[11] Both sections also provide that the court can reduce the amount in the trust if the court determines "that the value of the trust property exceeds the amount required for the intended use."[12] This power to reduce the amount in the trust allows a court to prevent a trust from serving a capricious purpose. Under the common law, a trust

3 *See* Restatement (Second) of Trusts § 123, Reporter's Notes.

4 *See id.*

5 *Id.* § 123 cmt. c; Restatement (Third) of Trusts § 47(1).

6 Restatement (Second) of Trusts § 123 cmt. d; Restatement (Third) of Trusts § 47(2).

7 Restatement (Second) of Trusts § 124; Restatement (Third) of Trusts § 47(2).

8 *See* Unif. Trust Code § 408 cmt. (Unif. Law Comm'n 2010) ("This section and the next section of the Code validate so called honorary trusts."); *see also id.* § 409 cmt.

9 *Id.* §§ 408(a), 409 cmt.

10 *Id*. §§ 408(b), 409(2).

11 *Id*. §§ 408(a), 409(1).

12 *Id*. §§ 408(c), 409(3).

purpose could not be capricious, and some cases found devoting excessive amounts of property to a purpose was capricious.[13]

Given the relatively limited purposes of honorary trusts—care of animals, care of graves, a power to distribute property for benevolent purposes—restrictions to comply with the rule against perpetuities and the prohibition against capricious purposes make sense. For a trust intended to hold the assets of a business, with the purpose of managing the business, these restrictions are problematic. An amendment to Section 409 could simply remove these two restrictions,[14] but the restrictions may be appropriate for the types of purpose trusts for which the section was initially created. A better approach will be to create a new section for a new type of purpose trust—a stewardship trust. The new section can be limited to trusts holding assets for a business purpose and can provide a framework for the new type of trust.

II. Stewardship Trust – A New Type of Purpose Trust

A stewardship trust will be useful for a business that wants to transition to steward-ownership, the idea that the purposes of a business and not profit should drive decision-making and that people close to the business should control its management.[15] A stewardship trust can protect the mission of a business and prevent the sale of the business to outside buyers who might change or close the business. Two types of businesses, family businesses and mission-driven businesses, may find it useful. A new section added to the UTC could provide for a stewardship trust, to be used for steward-ownership.

The new section would require that a stewardship trust be created for a business purpose that could include both financial and non-financial benefits. For example, the mission of Organically Grown Company (OGC), an Oregon corporation, is "Promoting health through organic agriculture as a leading sustainable organization."[16] OGC's business purposes are to distribute organic produce to retailers in a manner that supports the environment, the farmers, the employees, and the communities in which the company operates. Steward-ownership means that

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13 Restatement (Third) of Trusts § 47(2) cmt. e (Am. Law Inst. 2003).

14 Delaware has taken this approach. Del. Code Ann. tit. 25, § 503(a) (2019).

15 For an explanation of steward-ownership, see generally *Steward-Ownership – Rethinking Ownership in the 21st Century*, Purpose Found. (2018), https://purpose-economy.org/wp-content/uploads/2019/05/PurposeBooklet_EN_150519_Digital.pdf.

16 *The OGC Way: The pillars of our organizational culture*, Organically Grown Co., https://www.organicgrown.com/about/organizational-vitality/ (last visited Oct. 9, 2019).

OGC management will make decisions with all of those purposes in mind and will not make decisions solely based on profits.[17]

A stewardship trust can hold a business as a way of pursuing its purpose, and the expectation is that a stewardship trust will hold interests in a business organized as a corporation, partnership, or other legal entity. For example, a trustee would hold legal title to the voting shares of a business organized in corporate form. The trustee will act as a fiduciary, but the trust will be a directed trust.

In addition to a trustee, a stewardship trust will have a trust enforcer, an idea that comes from Sections 408 and 409. The trust enforcer will enforce the purposes of the trust and will act as a fiduciary. Under the new section, the trust enforcer will not be a beneficiary but will have the rights of a qualified beneficiary and will therefore be entitled to receive information from the trustee.

The new section will also require a trust stewardship committee (TSC). The TSC has the authority to exercise all rights of the trustee, and in particular will vote the shares of the business, elect the directors or other managers of the business, and oversee the administration of the business. The trust is a directed trust, with the TSC holding the powers to direct. The TSC must provide the trustee and trust enforcer with annual reports and any information necessary for them to carry out their duties. Like the trustee and the trust enforcer, the members of the TSC act as fiduciaries.

The TSC must have at least three members and can have as many more as the terms of the trust direct. If the trust is created for a family business, family members, employees, or people from the outside may serve on the TSC or elect its members. For a mission-driven business, the TSC may draw from groups of stakeholders such as employees, customers, community members, and investors.[18] The trust instrument can provide a process for electing or appointing members of the TSC, as well as for naming successor trustees and trust enforcers. If the trust instrument is silent, the statute provides a process.

The new section should also provide that the rule against perpetuities will not apply to a stewardship trust, so the trust can continue indefinitely. The new section will not include the provision from Sections 408 and 409 that gives a court authority to reduce the amount in the trust if it exceeds the amount necessary to meet the purposes of the trust. The removal of these two restrictions makes the stewardship trust a better

[17] OGC transitioned to steward-ownership in 2018, using a perpetual purpose trust that became the inspiration for the stewardship trust. *See* Purpose Found., *supra* note 15, at 83-84.

[18] OGC's committee draws from employees, farmers, customers, investors, and the community. *See* Purpose Found., *supra* note 15, at 83.

option for a trust holding a business, while the requirements and default rules in the new section create a structure that will support the business. The requirements for a stewardship trust also mean that the types of trusts that Section 409 was intended to cover will still use that section and not the new section.

III. Benefits for Family Businesses and Mission-Driven Businesses

An entrepreneur with a successful business may lack family members with the ability or interest to take over the business. Even if current family members want to work in the business, they may not be the best candidates for leadership of the company. Further, their future divorces or other discord within the family could threaten the continuation of the business over time.[19] The business owner may want to keep control of the management of the business in the hands of insiders but not limit control to family members. The owner may want to avoid a sale to an outsider and may want to keep the business, its jobs, and its values in the community.

The founders of a mission-driven business may want the business's mission to continue indefinitely, without the threat of sale or the worry that buyers will change the focus of the mission to profits above all else.[20] A stewardship trust can protect the mission, and the company can use nonvoting preferred stock to raise funds to buy out existing shareholders.[21]

For both family businesses and mission-driven businesses, a stewardship trust provides a means to address the owners' concerns. The structure described in this essay was enacted into law in Oregon in the 2019 legislative session.[22] The Oregon statute provides a good model for a new section for the UTC.

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19 *See* Alexander A. Bove Jr., *The Purpose Trust Has a New Purpose*, 33 Prob. & Prop., July/Aug. 2019, at 40, 42.

20 *See* Purpose Found., *supra* note 15, at 76-90 (providing case studies of businesses using different legal structures to accomplish succession planning for their steward-owned businesses).

21 See *id.* at 30-39 for an explanation of financing options.

22 H.B. 2598, 2019 Leg., 80th Sess. (Or. 2019). I worked with Natalie Reitman-White, Vice President of Organizational Vitality and Trade Advocacy for Organically Grown Company, and Steven G. Bell and Penny Serrurier, attorneys with Stoel Rives LLP, to draft the stewardship trust statute. Bell and Serrurier had helped OGC create a perpetual purpose trust using Delaware law.