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Trusts - The Fiduciary Aspects of Estate Corporations

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TRUSTS—THE FIDUCIARY ASPECTS OF ESTATE CORPORATIONS— With the ever-increasing reliance being placed on the corporate form by modern business, it is no longer unusual for an executor or testamentary trustee to discover that the estate or trust assets include the controlling shares in a close corporation, or that the testator's will directs him to form a corporation for the purpose of taking over and continuing the testator's business or investment holdings. Such corporations are commonly given the name "estate corporations," with the special type formed after testator's death further termed "post mortem" corporations. It is the purpose of this comment to examine the existing law with regard to estate corporations, in the hope of providing a guide for persons contemplating contact with them.

I. *Introduction*

There may be various reasons why an individual would prefer that his business interests be continued after his death. These might include difficulty in evolving a plan providing for the profitable disposal of the interest before or shortly after death, or the desirability of retaining the interest for the benefit of his family, especially if the business is relatively secure, yields a high rate of return, and is blessed with competent management.[1] The corporate form may be chosen for the continued operation in order to assure ease of administration, limitation of liability, simplicity in dealing with third parties, continuity of management, avoidance of partition, and quite possibly to obtain tax benefits.

The realization of these advantages depends in varying degree upon the ability of the corporate entity to separate the administration of the business interests from the confinements of ordinary trusteeship. Just how far this may be done will often be the first question raised by the individual considering the use of a

[1] See Durand, "Changing Concepts of Trust Investments," 95 TRUSTS AND ESTATES 907 (1956).

corporation in his estate plan. But because the area of estate corporations requires consideration of both the law of trusts and that relating to corporations, it must be recognized that the law applicable to one or the other may not be automatically relied on to supply all the answers. For the same reason, the executor or trustee, realizing that competing legal principles are involved, will be wary of accepting the fiduciary position unless his duties, rights and sanctions have been satisfactorily defined. In other words the fiduciary desires primarily that his responsibilities and obligations in respect to the estate corporation be plainly marked so that an open corridor of "proper" action is available to him. Absent such specification, the fiduciary, particularly the corporate trustee, may decline the trust and thus frustrate the decedent's plans. Although it was declared some twenty years ago that a settled body of law would undoubtedly be formulated to control this subject,[2] this prediction has not yet been fulfilled to the extent of permitting the law to be stated in terms of anything approaching clear cut rules.

II. *Fiduciary Responsibilities of the Trustee*

Initially it will be necessary for the newly-appointed fiduciary to establish his right to form a post mortem corporation or to continue the corporation previously organized by the decedent.[3] If he should proceed without valid authorization, he will be inviting probable surcharge for any and all losses sustained. The question of what amounts to proper authorization is essentially the same whether the business sought to be continued is incorporated or unincorporated, and is susceptible to firmer generalization than most of the problems encountered in estate corporations. Thus it may be said that in the absence of the consent of all beneficiaries and creditors, authority for prolonged continuation of the corporate business or for the formation of a post mortem corporation must be found in the clear expressions of the will.[4] In one

[2] See Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937).

[3] See generally Adelman, "The Power to Carry on the Business of a Decedent," 36 MICH. L. REV. 185 (1937); Polasky, "Planning for the Disposition of a Substantial Interest in a Closely Held Business," 44 IOWA L. REV. 83 (1958).

[4] Ibid. See also Durand, "Changing Concepts of Trust Investments," 95 TRUSTS AND ESTATES 907 (1956); P-H WILLS, ESTATES AND TRUST SERV. ¶2193.1 at p. 2195 (1950); 27 VA. L. REV. 497 (1941); Wachtler, "Continuance of a Decedent's Business by His Personal Representative in New York," 7 INTRA. L. REV. 40 (1940); Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937).

corporate situation—where the controlling shares are bequeathed to a trustee in trust—the court may imply a right to continue, whereas such right will not ordinarily be implied in the case of a non-corporate business.[5]

Assuming that authority for continuation is present and exercised, it is commonly held that the executor or trustee has an obligation to the beneficiaries to take an active part in the operation of the corporate affairs, including the duty to control the board of directors if and when possible.[6] It follows that the fiduciary with control of the estate corporation will normally be serving not only as a trustee or executor but also as an officer or director of the corporation. It is this dual capacity that gives rise to most of the major problems in the area.

As suggested, the duty to be active in corporate management will ordinarily be meaningful only if the trust has "control" of the corporation, and ownership to a lesser degree will raise few peculiar problems.[7] But to find this "control" it is not always necessary that the estate or trust hold the majority stock interest in its own right. If the fiduciary individually owns some, but less than a majority, of the corporate stock, his holdings are added to those of the trust in determining whether the estate has the majority necessary for "control."[8] Some courts would go a step further and attribute control to the trust when the fiduciary as an individual owns the majority stock in any corporation in which

[5] In re Berri, 130 Misc. 527, 224 N.Y.S. 466 (1927); Elias v. Schweyer, 13 App. Div. 336, 43 N.Y.S. 55 (1897). See P-H WILLS, ESTATES AND TRUST SERV. ¶2193.1 at p. 2197 (1950); 27 VA. L. REV. 497 (1941).

[6] See P-H WILLS, ESTATES AND TRUST SERV. ¶2193.1 at p. 2199; 27 VA. L. REV. 497 (1941). Both articles rely partially on Elias v. Schweyer, 13 App. Div. 336, 43 N.Y.S. 55 (1897), and In re Fidelity Loan, Trust & Guaranty Co., 23 Misc. 211, 51 N.Y.S. 1124 (1898), in which the trustee was already a director-officer and the question was whether it was proper for him to serve in such capacity. Trachtman, "Closely Held Businesses," 90 TRUSTS AND ESTATES 668 (1951), suggests that if the fiduciary believes in the competence of present management and keeps himself thoroughly informed, he need not serve as director. It is probable that the director's actions would still be imputed to the trustee in any action for breach of trust so that the end result would probably be the same.

[7] Generally the courts consider any thing over a 50% stock ownership as "control." Presumably the considerations might be different if the corporation permitted cumulative voting.

[8] In re Auditore's Estate, 136 Misc. 664, 240 N.Y.S. 502 (1930); Dailey v. Wright, 94 Md. 269, 51 A. 38 (1902); In re Davidson's Estate, 89 N.Y.S. (2d) 224 (1949); Pyle v. Pyle, 137 App. Div. 568, 122 N.Y.S. 256 (1910); In re Rappaport's Estate, 96 N.Y.S. (2d) 741 (1950); In re Witkind's Estate, 167 Misc. 885, 4 N.Y.S. (2d) 933 (1938). See generally Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937); 161 A.L.R. 1038 (1946).

the trust or estate also has some interest.[9] Others insist that the trustee who independently owns a majority interest is free to vote that stock and take action as a director without primary regard for the estate's interests.[10]

The usual fiduciary duty imposes on the trustee an obligation of absolute fidelity to the beneficiary's interest, and he will not be permitted to place himself in a position where interests of his own or of others may conflict with that of his beneficiary.[11] The possibility of extending this duty beyond its traditional context furnishes the questions of primary importance in the area of estate corporations; whether expressly[12] or impliedly, the courts dealing with the individual acting both as trustee and director have sometimes ignored the corporate form of doing business[13] and extended this duty of the trustee to act solely for the beneficiary so as to apply it also to the trustee-director's[14] actions as a corporate director.[15] When, if ever, this should be done to protect the beneficiary, and when the corporate form should be preserved in order to protect its integrity and usefulness is the question to which the courts must furnish an answer.

A corporate director's wrongful act customarily creates a single right of action in the corporation, to be enforced through

9 In re Barrett's Estate, 168 Misc. 937, 6 N.Y.S. (2d) 689 (1938).

10 E.g., Matter of Sullivan, 169 Misc. 16, 6 N.Y.S. (2d) 783 (1938), affd. 255 App. Div. 1008, 8 N.Y.S. (2d) 533 (1938).

11 For a valuable discussion of the fiduciary duty, see Hoover, "Basic Principles Underlying the Duty of Loyalty," 5 CLEVE.-MARSH. L. REV. 7 (1956). Also see 1 SCOTT, TRUSTS §2.5 (1939).

12 Erickson v. Starling, 233 N.C. 539, 64 S.E. (2d) 832 (1951); In re Doelger's Estate, 164 Misc. 590, 299 N.Y.S. 565 (1937), revd. 254 App. Div. 178, 4 N.Y.S. (2d) 334 (1938), affd. In re Doelger's Will, 279 N.Y. 646, 18 N.E. (2d) 42 (1938); Pyle v. Pyle, 137 App. Div. 568, 122 N.Y.S. 256 (1910).

13 As a matter of terminology it may be inaccurate to suggest that a court is "ignoring the corporate form" merely by applying trust rules to the actions of the trustee-director. In this view of the matter, no question of "corporate form" is ever reached since the trust rules merely circumscribe the discretion of the individual director because of his additional legal status as trustee. On the other hand, this phrase can be meaningfully employed to describe any situation in which the court, for one reason or another, refuses to apply the rule that would govern the normal corporate situation, and instead adopts some other rule in order to bring about a desired result. As suggested above, where there is a conflict between the rule applicable to corporate directors and that applicable to trustees, the courts frequently will refuse to apply the corporate rule. This is what is meant here by "ignoring" or "avoiding" the corporate form.

14 Throughout this comment the words "trust" and "estate" are used interchangeably. "Director" and "officer" will also not be distinguished since for purposes of examining problems peculiar to estate corporations, there are no useful distinctions between the two.

15 See generally Durand, "Changing Concepts of Trust Investments," 95 TRUSTS AND ESTATES 907 (1956); Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937).

a stockholder's derivative suit. But when the corporation involved is an estate corporation, it seems settled, at least in New York, that such misconduct gives rise to separate and independent causes of action in both the corporation and the trust beneficiaries.[16] The beneficiaries' action will be based on breach of trust and the recovery from the trustee will be an amount measured by the reduction in value of the estate's stock caused by his wrongful act as director.[17] From the language used, these courts seem willing to carry this concept of liability to the extent of allowing two full and separate recoveries. However, in none of these cases had there been a previous recovery,[18] so the question of double recovery was not directly in issue. It would seem that the rationale underlying allowance of two recoveries is sound, at least when there are minority interests in the corporation independent of the trust holdings. If a derivative suit were instituted after the beneficiaries had already recouped their loss, anything less than judgment for the full damage to the corporation could well be destructive of the rights of such minority stockholders. Anything collected in this action would belong to the corporation as a whole so that if the beneficiaries' previous recovery were deducted from the later judgment, the portion of the amount remaining which would accrue to the minority would not represent its full damages.

An even greater departure from traditional corporate concepts than two recoveries for one wrong is the possibility that application of fiduciary rules to estate corporations will mean that acts of the trustee-director which are perfectly proper and beneficial from a corporate standpoint may still be a breach of trust because they are not strictly in the immediate interest of the life beneficiary.[19] Conversely, the action most desirable to this income beneficiary may be undesirable from an overall corporate viewpoint, because it raises the threat of liability in a derivative

16 See Matter of Auditore, 249 N.Y. 335 (1928); In re Gerbereux's Will, 148 Misc. 461, 266 N.Y.S. 134 (1933); In re Greenberg's Estate, 149 Misc. 275, 267 N.Y.S. 384 (1933). The result in other states would likely be the same though the cases are not as plentiful. Compare In re Clarke's Will, 204 Minn. 574, 284 N.W. 876 (1939), with Rossi v. Davis, 345 Mo. 362, 133 S.W. (2d) 363 (1939).

17 In re Auditore's Estate, 136 Misc. 664, 240 N.Y.S. 502 (1930). See P-H WILLS, ESTATES AND TRUST SERV. ¶2193.1 at p. 2204 (1950).

18 In In re Auditore's Estate, 136 Misc. 664, 240 N.Y.S. 502 (1930), there was an outstanding judgment from a previous derivative suit but it was no longer collectible.

19 E.g., notes 30 and 40 infra.

suit. As an example, the establishment of corporate reserves is necessary to the general business interest of the corporation as an entity. But such reserves would be highly prejudicial to a life beneficiary interested only in income, and would be improper in the ordinary trust where no corporation is imposed. Thus it is obvious that the trustee may be faced with competing interests, both of which it will be impossible to satisfy. Where such a conflict exists the court may sometimes feel that it would be justifiable to follow the fiduciary duty through the corporate veil and require the trustee-director to adhere to conduct most favorable to the beneficiary. But while the possibility of a disregarding of form should be considered when the estate plan is being formulated, it should cause few problems to the enlightened trustee holding the entire issue of corporate stock. If he consistently acts in the interest of the immediate beneficiaries, to the extent required by usual trust rules, there will be no one with standing to object to his conduct. The fact that the trustee has not always adhered to this course has been the cause of much needless litigation. A real problem for the fiduciary does arise, however, when the trust or estate holds less than all the corporate stock. It may be argued that the majority stockholders and directors elected thereby are free to plan their actions solely with regard to what is most beneficial to the majority—in this case the trust. If this is true, the trustee who looks only to the beneficiaries' advantage would again be safe. However, the more modern approach has often been to attach a fiduciary aspect to the corporate director-corporate minority relation and consequently to find a duty on the part of the director to act in the best interest of the corporation as a whole.[20] If, then, the estate holds the controlling but not the entire stock, action taken in the interest of the trust may, in some instances, bring about an objection by the minority that such acts were not taken in the best interests of the corporation. Yet even in a jurisdiction recognizing responsibility to the minority stockholders, it would still be logically possible to brush aside the objections of some minority groups. If the court is willing to make an exception to the fiduciary duty where the minority takes its interest with notice that the estate is in control of the corpo-

[20] Lebold v. Inland Steel Co., (7th Cir. 1941) 125 F. (2d) 369, cert. den. 316 U.S. 675 (1941). See Elevator Supplies Co. v. Wylde, 106 N.J. Eq. 163, 150 A. 347 (1930). But see Kirwan v. Parkway Distillery, 285 Ky. 605, 148 S.W. (2d) 720 (1941).

ration, then it could be reasoned that the minority in a post mortem corporation or a minority which acquired its stock subsequent to the testator's death has such notice and is bound by it.[21] This notice argument, however, would frequently be inapplicable to a subsequent purchaser, since he seldom would have actual notice, and it almost certainly could be of no help where there is an independent minority who obtained its stock before the testator's death.

In general the courts have not yet been squarely faced with the spectre of conflicting fiduciary interests, so any observation as to its effect is largely speculation. Only a few decisions have even mentioned the problem,[22] and in these cases the problem was not directly in issue. Nevertheless, the possibility of an objecting minority raises important issues that may in the future be of major concern to the courts and should be considered along with any examination of the scope of the trustee-director's duty to the trust.

III. *Areas of Conflict*

A. *Retention of Corporate Earnings.* When the testator expresses his intent in the will as to how the estate corporation is to be conducted, the courts have been almost unanimous in holding the trustee-director bound to carry out those directions.[23] The rationale is usually that having taken his authority from the will, the trustee is estopped to deny the validity of instructions in that instrument.[24] If such directions are not in the best interest

21 See In re Doelger's Estate, 164 Misc. 590, 299 N.Y.S. 565 (1937), revd. 254 App. Div. 178, 4 N.Y.S. (2d) 334 (1938), affd. In re Doelger's Will, 279 N.Y. 646, 18 N.E. (2d) 42 (1938). See Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937).

22 In re Doelger's Estate, 164 Misc. 590, 299 N.Y.S. 565 (1937), revd. 254 App. Div. 178, 4 N.Y.S. (2d) 334 (1938), affd. In re Doelger's Will, 279 N.Y. 646, 18 N.E. (2d) 42 (1938); In re Trust under Will of Koffend, 218 Minn. 206, 15 N.W. (2d) 590 (1944); In re Peabody's Estate, 218 Wis. 541, 260 N.W. 444 (1935); 99 A.L.R. 956 (1935). In In re Hubbell's Will, 90 N.Y.S. (2d) 74, affd. 276 App. Div. 134, 93 N.Y.S. (2d) 555 (1949), revd. 302 N.Y. 246, 97 N.E. (2d) 888 (1951), the Surrogate's Court partially based its decision on protection of the minority's rights but the decision was subsequently reversed.

23 In re Doelger's Estate, 164 Misc. 590, 299 N.Y.S. 565 (1937), revd. 254 App. Div. 178, 4 N.Y.S. (2d) 334 (1938), affd. In re Doelger's Will, 279 N.Y. 646, 18 N.E. (2d) 42 (1938); Elger v. Boyle, 69 Misc. 273, 126 N.Y.S. 946 (1910); Farmers Loan & Trust Co. v. Pierson, 130 Misc. 110, 222 N.Y.S. 532 (1927); In re Trust under Will of Koffend, 218 Minn. 206, 15 N.W. (2d) 590 (1944). But see Green v. Philadelphia Inquirer Co., 329 Pa. 169, 196 A. 32 (1938).

24 Elger v. Boyle, 69 Misc. 273, 126 N.Y.S. 946 (1910); Farmers Loan & Trust Co. v. Pierson, 130 Misc. 110, 222 N.Y.S. 532 (1927); In re Trust under Will of Koffend, 218 Minn. 206, 15 N.W. (2d) 590 (1944).

of the corporation and a pre-existing minority is present to contest, it might be doubted that the decedent's orders should still be controlling. To allow the orders to control in this situation would give the decedent power to take action through testamentary directions that he could not have taken as a director during life. However, there is no authority to this effect and the estoppel argument can still be urged against the fiduciary. More often the will does not contain instructions and the question then becomes whether the court will choose to uphold or look through the corporate entity as a matter of policy or implied intent. The problem is most vividly apparent when the trustee's action in the interest of the beneficiaries will result in non-recognition of one of those elements thought of as distinguishing the corporation from other business forms. One of these characteristics—the right of a corporation to retain a part of its earnings, for depreciation reserves or otherwise—has been the cause of a large part of the litigation in the estate corporation area and has arisen in several different settings.

1. *Corporate Debts.* In 1937 two widely cited New York decisions involving wholly-owned estate corporations invalidated the use of corporate income to pay to the estate a pre-existing debt of the corporation due the testator.[25] While holding that such payments were in violation of the New York statute against accumulations of trust income, since income then became part of the trust res over which the income beneficiaries had no claim, it was not denied that this was merely a conclusion reached after a decision based on policy or implied intent that the corporate form should give way in favor of the income beneficiary's claim to all corporate income.[26] The corporation was likened to a "repository for assets" and it was concluded that under the circumstances corporate income can be treated as ordinary trust income.[27] While the court in *In re Adler's Estate*[28] intimated that the will terms may have shown testator's intent not to consider the corporation as a

[25] In re Adler's Estate, 164 Misc. 544, 299 N.Y.S. 542 (1937); In re McLaughlin's Estate, 164 Misc. 539, 299 N.Y.S. 559 (1937).

[26] See 38 COL. L. REV. 942 (1938); 47 YALE L. J. 1026 (1938).

[27] In re Adler's Estate, 164 Misc. 544, 299 N.Y.S. 542 (1937); In re McLaughlin's Estate, 164 Misc. 539, 299 N.Y.S. 559 (1937). See Durand, "Changing Concepts of Trust Investments," 95 TRUSTS AND ESTATES 907 (1956), to the effect that in the area of principal and income, it is not unusual for the wholly owned corporation to be treated as an administrative device.

[28] 164 Misc. 544, 299 N.Y.S. 542 (1937).

separate entity, neither decision was actually based on the discovery of an express intent but resulted more from a policy favoring the income beneficiary. Under these circumstances the existence of a minority interest would not supply any strong additional arguments for an opposite result. Since it otherwise would have no right to share in the income involved, the disallowance of the payments and the implication that such funds must be paid out as dividends causes no harm to the minority.

A suggestion was made in the *Adler* case, and in other cases as well, that the tendency to favor the income beneficiary over the interests of the corporation is more prevalent where the trustee-directors are also remaindermen.[29] This factor, however, even if considered by the court, will probably not be controlling because the courts have generally tended to favor the income beneficiaries even where the the trustees are not remaindermen.

2. *Reserves.* Where corporate ownership is entirely vested in the estate or trust and there is no history of income reserves from which an intent that they be continued could be clearly implied, most cases have found the establishment of reserves from corporate income to be improper.[30] The Pennsylvania decisions alone have clearly indicated their disapproval of this patent disregard of the corporate entity.[31] The courts have generally not attempted to justify such disregard on an implied intent theory, so that their results apparently flow from a pure policy determination favoring the income beneficiary.[32] If the reasoning were based on the implied intent of the testator for the corporation to be only an administrative device, it would seem that ordinarily it could as easily be inferred that he would have desired the corporation to be empowered with all the normal corporate attributes.[33] This

[29] See 47 YALE L. J. 1026 at 1031 (1938).

[30] In re Adler's Estate, 164 Misc. 544, 299 N.Y.S. 542 (1937); In re McLaughlin's Estate, 164 Misc. 539, 299 N.Y.S. 559 (1937). Both of these cases indicated they might exclude temporary improvements made by the trustee which are not likely to last beyond the income beneficiary's interest. In re Hubbell's Will, 90 N.Y.S. (2d) 74 (1948), affd. 276 App. Div. 134, 93 N.Y.S. (2d) 555 (1949), revd. 302 N.Y. 246, 97 N.E. (2d) 888 (1951); Rossi v. Davis, 345 Mo. 362, 133 S.W. (2d) 363 (1939). *Contra,* Boyle v. John Boyle & Co., 136 App. Div. 367, 120 N.Y.S. 1048 (1910), rehg. den. 131 N.Y.S. 1105 (1911), affd. 200 N.Y. 597, 94 N.E. 1092 (1911).

[31] Goetz's Estate (No. 1), 236 Pa. 630, 85 A. 65 (1912); Green v. Philadelphia Inquirer Co., 329 Pa. 169, 196 A. 32 (1938).

[32] See 38 COL. L. REV. 942 (1938).

[33] This would probably not be true if the facts show that the testator created the corporation before death but continued to deal with the corporate assets as his individual property.

has been the reasoning used by the Pennsylvania courts[34] and at least one New York decision[35] in holding the establishment of reserves to be proper. In any of the retention of earnings cases, it could also be argued that the court should infer a different intent according to whether the corporation in question comprises a going business or is an incorporation of the testator's investments.[36] If the assets consist of investments, it may be probable that the corporation was formed merely as an instrument to conduct the individual's affairs with little thought of its ever being an operating entity with all the characteristics of such entities.

If the decisions disallowing reserves are based purely on policy, it is very doubtful that such policy would be considered potent enough to overcome express will directions in favor of reserves. It would seem more likely that the policy against reserves would be held applicable only where testator's intent is unknown, although this would undoubtedly force New York to reappraise its accumulations statute.[37] Besides going against most of the authority and finding no policy or intent opposed to corporate reserves,[38] the Pennsylvania courts have been unique in suggesting, by way of dicta, that typical corporate rights such as retention of earnings could not be overcome by contrary will expressions.[39]

The situation where there is an independent minority interest presents greater problems for the trustee faced with the question whether to set up corporate reserves. The risk to an alert fiduciary in that case is an inability to tell whether, in the absence of an intent expressed through testamentary instructions, the policy in favor of beneficiaries will be strong enough to overcome the justifiable interest of an independent minority in the establishment of reserves, or whether a paying out of all corporate income will create a cause of action in the corporation. Cases of this type are not numerous enough to indicate a trend, but if the minority

34 See note 31 supra.

35 Boyle v. John Boyle & Co., 136 App. Div. 367, 120 N.Y.S. 1048 (1910), reh. den. 131 N.Y.S. 1105 (1911), affd. 200 N.Y. 597, 94 N.E. 1092 (1911).

36 See 27 VA. L. REV. 497 (1941).

37 On its face the statute would be more clearly applicable where the will directs the establishment of reserves than in In re Adler's Estate, 164 Misc. 544, 299 N.Y.S. 542 (1937), and In re McLaughlin's Estate, 164 Misc. 539, 299 N.Y.S. 559 (1937), discussed at note 25 supra, since the court in those cases was somewhat reluctant to apply the statute because there was no specific order to accumulate.

38 See note 31 supra.

39 Ibid.

is not present and objecting, a court could cite cases involving wholly-owned corporations and strike down the reserves without actually considering the difference in problems.[40] If the court recognizes an obligation of directors to act for the good of the corporation as a whole, however, the real need for adequate corporate reserves would seem to present a very attractive case for the application of that doctrine. Furthermore, such an obligation could be used to uphold reserves even in the face of contrary directions in the will. There is little doubt that any non-trust holdings would be seriously damaged by a failure of the corporation to provide such reserves. And it should not logically affect the minority's rights that the testator as majority stockholder ordered the trustee-director to pay out all corporate income; the damage to the corporation would be the same.[41]

3. *Income Beyond Dividends.* The third and most obvious test of the estate corporation's right to retain earnings is presented by a beneficiary's claim to corporate income beyond that declared as dividends. Essentially this is but the next logical step after a decision on the propriety of corporate reserves, since it is unlikely that the court would disallow reserves unless it was willing to follow with a decree that all income must be paid out. However, it is easier to find authority for saying the beneficiary has no claim beyond declared dividends[42] than for permitting corporate reserves, and this may suggest a possible distinction between the two related areas. The ultimate effect on the corporate entity of ordering earnings to be paid out beyond dividends declared and of disallowing corporate reserves is probably no different. But since the right of the stockholder only to such income as is declared in dividends is one of the principal characteristics

[40] See In re Hilliard's Will, 164 Misc. 677, 299 N.Y.S. 788 (1937). But see In re Barrow's Will, 204 Misc. 339, 123 N.Y.S. (2d) 501 (1953), affd. 283 App. Div. 995, 130 N.Y.S. (2d) 914 (1954).

[41] Whether the policy of carrying out will directions would be subserved in this case is not a question allowing accurate generalization. In re Barrow's Will, 204 Misc. 339, 123 N.Y.S. (2d) 501 (1953), affd. 283 App. Div. 995, 130 N.Y.S. (2d) 914 (1954), a recent New York case involving a minority interest but no testamentary directions permitted corporate reserves, and this may indicate some recognition of minority rights. However, the opinion offers nothing to substantiate this, and it is just as likely that the court believed it was following the testator's intent.

[42] Boyle v. John Boyle & Co., 136 App. Div. 367, 120 N.Y.S. 1048 (1910), reh. den. 131 N.Y.S. 1105 (1911), affd. 200 N.Y. 597, 94 N.E. 1092 (1911); Dailey v. Wright, 94 Md. 269, 51 A. 38 (1902); In re Fidelity Loan, Trust & Guaranty Co., 23 Misc. 211, 51 N.Y.S. 1124 (1898); Goetz's Estate (No. 1), 236 Pa. 630, 85 A. 65 (1912); Green v. Philadelphia Inquirer Co., 329 Pa. 169, 196 A. 32 (1938).

generally thought of as distinguishing the corporation from other business forms, a claim to further income will more directly force the court to an immediate and open decision between recognition of the corporate form and the rights of the income beneficiary. This is true whether the corporation is wholly owned or is merely "controlled" by the trust. Therefore when an issue involves corporate rights and the court avoids directly facing the dividend question, as did the courts in many of the corporate reserve cases, it may decide the case without fully recognizing that a problem of ignoring the corporate form is involved.

Most of the cases disallowing an enlarged right in corporate earnings have concerned corporations less than wholly owned by the estate.[43] Whether or not this is a realization of the minority problem, it certainly shows a greater reluctance to treat such corporations as a mere device of administration. Again, in the dividend area, it seems that testamentary directions should not affect the strength of objections by independent owners. Yet the only authority for this proposition is dicta in certain Pennsylvania cases.[44]

B. *Corporate Salaries.* The propriety of payment of a corporate salary to a trustee-director over and above his compensation from the estate raises a problem slightly different from those previously examined, although it too could be analyzed as involving a failure to pay out all corporate earnings to the income beneficiaries. However, since the salary question directly concerns only the personal rights and obligations of the trustee, many courts would not even analyze this as a corporate entity problem.[45] Moreover, while this problem is still one of conflicting interests, it is perhaps more of a conflict of the beneficiary's interest with the fiduciary's personal interest than with the interest of the corporation as a whole.

It is not difficult to find a number of decisions disapproving corporate salaries paid to a trustee-director as being inconsistent with his fiduciary duty.[46] But in contrast to most of the other

43 Boyle v. John Boyle & Co., 136 App. Div. 367, 120 N.Y.S. 1048 (1910), reh. den. 131 N.Y.S. 1105 (1911), affd. 200 N.Y. 597, 94 N.E. 1092 (1911); Dailey v. Wright, 94 Md. 269, 51 A. 38 (1902); In re Fidelity Loan, Trust & Guaranty Co., 23 Misc. 211, 51 N.Y.S. 1124 (1898).

44 See note 31 supra.

45 See In re Steinberg's Estate, 153 Misc. 339, 274 N.Y.S. 914 (1934).

46 In re Grossman's Estate, 157 Misc. 164, 283 N.Y.S. 323 (1935), affd. 294 N.Y.S. 942 (1937). And see Elias v. Schweyer, 13 App. Div. 336, 43 N.Y.S. 55 (1897). Both of these cases

areas of estate corporations the trend, especially in more recent years, seems to be toward upholding such payments and consequently toward recognition of the corporate entity.[47] Most of the decisions finding a conflict of interests and disallowing the salary payments have reasoned that receipt of a corporate salary by the fiduciary will generate a personal interest in the continued existence of the corporation so that he would be unwilling to sell the estate's holdings even if a highly advantageous offer were received.[48] In several of these cases there were other acts of serious misconduct by the trustee[49] so that it is impossible to determine whether the salary question standing alone would have precipitated the same result.

Courts permitting corporate compensation are often the same courts that have denied the corporate right to retain income, and thus reluctance to look through the corporate veil has not been the basis for allowing the compensation. The earlier decisions often involved a trustee who was a salaried officer of the corporation before the testator's death, so it was not difficult to imply an intent that this salary should continue.[50] While such a finding of intent would always make it easier to uphold the salary, the

involved corporations wholly owned by the estate. Clark v. Clark, 167 Ga. 1, 144 S.E. 787 (1928); In re Hirsch's Estate, 116 App. Div. 367, 101 N.Y.S. 893 (1906), affd. 188 N.Y. 584, 81 N.E. 1165 (1907); Matter of Kirkman, 143 Misc. 342, 256 N.Y.S. 495 (1932); Pyle v. Pyle, 137 App. Div. 568, 122 N.Y.S. 256 (1910), all involving corporations less than wholly owned by the estate. And see 2 SCOTT, TRUSTS, 2d ed., §170.22 (1956).

47 In re Berri, 130 Misc. 527, 224 N.Y.S. 466 (1927); In re Davidson's Estate, 89 N.Y.S. (2d) 224 (1949); Lawrence v. Garner, 48 Hun (N.Y.) 618, 1 N.Y.S. 534 (1888); Rossi v. Davis, 345 Mo. 362, 133 S.W. (2d) 363 (1939); In re Smythe's Estate, 6 Misc. (2d) 130, 36 N.Y.S. (2d) 605 (1942), all involving wholly owned corporations. Dailey v. Wright, 94 Md. 269, 51 A. 38 (1902); In re Fidelity Loan, Trust and Guaranty Co., 23 Misc. 211, 51 N.Y.S. 1124 (1898); In re Gerbereux's Will, 148 Misc. 461, 266 N.Y.S. 134 (1933); In re Matchette's Estate, 183 Misc. 228, 49 N.Y.S. (2d) 561 (1944); In re Peabody's Estate, 218 Wis. 541, 260 N.W. 444 (1935); 99 A.L.R. 956 (1935); In re Teasdale's Estate, 261 Wis. 248, 52 N.W. (2d) 366 (1952); Williams v. Bond, 120 Va. 678, 91 S.E. 627 (1917); In re Witkind's Estate, 167 Misc. 885, 4 N.Y.S. (2d) 933 (1938), involving corporations less than wholly owned.

48 Elias v. Schweyer, 13 App. Div. 336, 43 N.Y.S. 55 (1897); In re Grossman's Estate, 157 Misc. 164, 283 N.Y.S. 323 (1935), affd. 294 N.Y.S. 942 (1937); In re Hirsch's Estate, 116 App. Div. 367, 101 N.Y.S. 893 (1906), affd. 188 N.Y. 584, 81 N.E. 1165 (1907); Pyle v. Pyle, 137 App. Div. 568, 122 N.Y.S. 256 (1910).

49 Clark v. Clark, 167 Ga. 1, 144 S.E. 787 (1928); In re Grossman's Estate, 157 Misc. 164, 283 N.Y.S. 323 (1935), affd. 294 N.Y.S. 942 (1937); In re Hirsch's Estate, 116 App. Div. 367, 101 N.Y.S. 893 (1906), affd. 188 N.Y. 584, 81 N.E. 1165 (1907); Matter of Kirkman, 143 Misc. 342, 256 N.Y.S. 495 (1932).

50 In re Berri, 130 Misc. 527, 224 N.Y.S. 466 (1927); Lawrence v. Garner, 48 Hun (N.Y.) 618, 1 N.Y.S. 534 (1888). And see 2 SCOTT, TRUSTS, 2d ed., §170.22 (1956), citing many cases.

later decisions clearly do not rely on prior corporate service. The decisive factor is the court's feeling that the extra services involved in running a corporation deserve additional compensation and that any potential conflict of interests is so remote that it may be ignored until it is actually shown to have affected the fiduciary's conduct.[51] It should be noticed, however, that the mere allowance of a corporate salary does not necessarily mean that the corporate entity is in theory left untouched. In Wisconsin, for example, trustees' salaries are measured by a standard of "reasonableness." When this problem was before it, the Wisconsin court simply added the corporate and trust salaries of the fiduciary and then decided that since the total was a reasonable trustee's compensation, the payment was proper.[52] On the other hand, New York fixes trustees' salaries as a percentage of sums received and paid out and of trust income accounted for,[53] so that any salary paid as director will be in addition to the statutory maximum for trustees. Therefore, to allow the extra compensation the court must treat the corporation as a separate body. But even if the corporate entity is generally fully recognized, it seems safe to say that the policy permitting corporate salaries is not so strong that it would overcome contrary will directions.[54]

Under limited circumstances it is possible that a minority interest might also object to corporate salaries, so it may again be profitable to distinguish the wholly-owned corporation from that only "controlled" by the trust. Under the New York approach, the independent stockholders might argue that since the trustee is receiving his full statutory compensation from the estate, the additional sums are an unnecessary expenditure of corporate funds, part of which would otherwise accrue to the stockholders. Yet this seems a rather weak argument, not only because it in a sense calls for disregard of the entity, but also because reasonable compensation for actual services cannot realistically be termed unnecessary expense. A somewhat stronger objection could arise under the Wisconsin view unless the court is careful in its analysis. The totaling device could make a trustee-director's overall

51 See note 45 supra. And see 27 VA. L. REV. 497 (1941).

52 In re Peabody's Estate, 218 Wis. 541, 260 N.W. 444 (1935); 99 A.L.R. 956 (1935); In re Teasdale's Estate, 261 Wis. 248, 52 N.W. (2d) 366 (1952).

53 N.Y. Surrogates Court Act, §285.

54 In re Stulman's Will, 146 Misc. 861, 263 N.Y.S. 197 (1933). And see P-H WILLS, ESTATES AND TRUSTS SERV., ¶2193.1 (1950).

compensation "reasonable" and proper even where the corporation was bearing a greater proportion of the salary than the fiduciary's services to it would ordinarily justify.[55]

C. *Accounting.* Whenever in a trustee's accounting proceeding the beneficiaries of the estate or trust demand a full disclosure of corporate records and activities, another area of conflict between the interests of the beneficiaries and the interest of the corporation as a whole is presented. Unlike the conflict raised by retention of corporate income, however, an accounting does not put in question a characteristic thought of as basic to the ordinary corporation. Probably for this reason the decisions in this area provide more certainty. Where the estate has held anything over 50 percent of the corporate stock, the courts have been close to unanimity in treating the trustee-director's actions as director as a part of his duties as trustee and thus requiring a disclosure of corporate records and activities.[56] If the estate owns less than all the corporate stock, some,[57] but not all,[58] of these courts would apparently require an allegation of wrongdoing by the trustee before ordering the disclosure. If the trust has complete ownership, the only persons that could be damaged by an open publication of corporate information are the beneficiaries themselves. However, an existing independent minority certainly may contend that an accounting decree which permits disclosure of confidential corporate operations will be harmful to the corporation.[59] But because an accounting is neither as immediately harmful

[55] It is probable that "reasonable" will be given a broad construction and doubtful that the court will be willing to define too closely what part of a reasonable total should be allowed for corporate services.

[56] Farmers Loan & Trust Co. v. Pierson, 130 Misc. 110, 222 N.Y.S. 532 (1927); In re Kadison's Estate, 265 App. Div. 870, 37 N.Y.S. (2d) 909 (1942); In re Steinberg's Estate, 153 Misc. 339, 274 N.Y.S. 914 (1934), involving wholly-owned corporations. In re Davidson's Estate, 89 N.Y.S. (2d) 224 (1949); Erickson v. Starling, 233 N.C. 539, 64 S.E. (2d) 832 (1951); In re Greenberg's Estate, 149 Misc. 275, 267 N.Y.S. 384 (1933); In re Hubbell's Will, 90 N.Y.S. (2d) 74, affd. 276 App. Div. 134, 93 N.Y.S. (2d) 555 (1949), revd. 302 N.Y. 246, 97 N.E. (2d) 888 (1951); In re Rappaport's Estate, 96 N.Y.S. (2d) 741 (1950); In re Witkind's Estate, 167 Misc. 885, 4 N.Y.S. (2d) 933 (1938), all "controlled" by the estate or by the trustee because of the estate stock. But see In re Browning's Will, 258 App. Div. 621, 17 N.Y.S. (2d) 557 (1940). And see 15 A.L.R. (2d) 11 (1951). It should not matter that the minority interest is held by the fiduciary but this may affect the court's thinking.

[57] See, e.g., In re Paddock's Estate, 186 Wis. 544, 203 N.W. 347 (1925); In re Stewart's Estate, 167 Misc. 361, 3 N.Y.S. (2d) 985 (1937).

[58] See, e.g., In re Rappaport's Estate, 96 N.Y.S. (2d) 741 (1950); In re Witkind's Estate, 167 Misc. 885, 4 N.Y.S. (2d) 933 (1938).

[59] Durand, "Changing Concepts of Trust Investments," 95 TRUSTS AND ESTATES 907 (1956).

to the "corporation" nor as patently in disregard of the entity as is a disposal of all income, and because of the real need for keeping the fiduciary's actions open to inspection, the minority would probably have trouble impressing its argument on the court. There have been almost no cases mentioning the problem and none allowing it to prevent an inspection of corporate affairs.[60]

Traditionally the courts have held that if the individual trustee and the estate together own only a minority interest, or if the fiduciary has control independent of the estate stock, beneficiaries have no right to demand an accounting which includes disclosure of corporate records.[61] The usual rationale has been that the corporate acts cannot be considered to be those of the trustee and the trustee is not in a position to acquire control of the corporate records. Because of such reasoning, and probably because of many peaceful years without complaint by non-estate interests, some recent decisions seem to take the further step of allowing an inspection of corporate records by minority estate interests at least where the trustee is in fact in a position to procure the records.[62] These cases may try to support their result by stating that the inspection is a limited one only. But where the "limit" is an inspection of all records necessary to determine if there has been fraud or wrongdoing by the fiduciary, it is actually no "limit" at all.[63] Despite a justifiable desire to protect the beneficiaries of a trust against the wrongdoing trustee, this could prove to be a serious invasion of the majority's interests in situations where disclosure of corporate records might be harmful to the interests of the corporation as a whole.

D. *Creditors.* In general, the courts have been rather liberal in crossing over and extinguishing the lines between the trust and the wholly-owned estate corporation in order to aid the credi-

60 In re Hubbell's Will, 90 N.Y.S. (2d) 74, affd. 276 App. Div. 134, 93 N.Y.S. (2d) 555 (1949), revd. 302 N.Y. 246, 97 N.E. (2d) 888 (1951), used such an argument to disallow an accounting in the lower court but the decision was reversed. See also In re Ebbets' Estate, 149 Misc. 260, 267 N.Y.S. 268 (1933).

61 In re Ebbets' Estate, 149 Misc. 260, 267 N.Y.S. 268 (1933); In re Ebbets' Will, 190 Misc. 821, 76 N.Y.S. (2d) 36 (1947); Matter of Sullivan, 169 Misc. 16, 6 N.Y.S. (2d) 783 (1938), affd. 255 App. Div. 1008, 8 N.Y.S. (2d) 533 (1938); In re Wainwright's Estate, 55 N.Y.S. (2d) 303 (1945). But see In re Barret's Estate, 168 Misc. 937, 6 N.Y.S. (2d) 689 (1938).

62 In re Murray's Will, 88 N.Y.S. (2d) 579 (1949); In re Shehan's Will, 285 App. Div. 785, 141 N.Y.S. (2d) 439 (1955), rearg. den. 286 App. Div. 953, 143 N.Y.S. (2d) 668 (1955).

63 Ibid.

tors of either.[64] In view of the general attitude of the judiciary in the estate corporation field, such a result is not surprising where the estate owns the entire corporate interest. Certainly, however, no court should go so far as to allow an estate creditor to enforce his claim against a corporation with an independent minority interest.[65]

IV. *Conclusion*

In the broad area of estate corporations there has not as yet been sufficient litigation to provide a quantity of established rules. It appears that only the courts of New York have considered a substantial number of such cases, and even there the results cannot be termed conclusive. It seems likely that future years will produce an increased volume of decisions on this complex subject, with some of them reaching into the still untouched area of conflicting fiduciary duties. When this does occur, some of the past decisions may be less than helpful unless the court is careful to analyze the various and distinct problems involved.

At present the picture is one of no great reluctance to ignore the corporate form and apply traditional trust rules to corporate action whenever the court feels that general policy or the testator's intent calls for such result. This is certainly the case where the corporation is wholly owned by the trust, and seems only slightly less true where at least a controlling interest is so owned. In accordance with this approach, some courts may indicate a willingness to advise in advance of the propriety of particular corporate action, although they may refuse to suggest the details of the action.[66] Helpful perspective may be gained if it is recognized that there is probably a trend in all sections of American law not to let the corporate form interfere with what is believed to be a correct result.[67]

[64] See In re Daly, 158 Misc. 659, 287 N.Y.S. 957 (1935), affd. 246 App. Div. 759, 283 N.Y.S. 929 (1935), where the corporate creditor was allowed to sue the estate; In re George's Will, 256 App. Div. 270, 9 N.Y.S. (2d) 533 (1939), where payments by the corporation to an estate creditor were permitted; In re Lesser's Estate, 154 Misc. 364, 277 N.Y.S. 123 (1935), where sums due the corporation were set off against the creditor's claim against the estate.

[65] In In re Abramowitz' Estate, 170 Misc. 68, 9 N.Y.S. (2d) 846 (1939), the estate owned 24⅓ out of the 25 corporate shares, and the estate creditor was allowed to enjoin improper corporate action that would have destroyed the corporate assets. The court seemed to treat the corporation as being wholly owned.

[66] See, e.g., In re Pulitzer's Estate, 139 Misc. 575, 249 N.Y.S. 87 (1931).

[67] See STEVENS, PRIVATE CORPORATIONS, 2d ed., §18 (1949); Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937).

Most articles in this field have concluded that the estate corporation serves a highly useful function and that its usefulness should not be slowly impaired by application of trust rules to corporate action.[68] This is probably true, but in some situations the court could hardly be criticized for allowing basic concepts of fairness to overcome arguments based purely on form. And it also should be recognized that a limited disregard of corporate entity may not greatly endanger the utility of the estate corporation. At least as great a threat to the estate corporation is an uncertainty in treatment that would not only lead to disuse but would cause qualified trustees to refuse the trust rather than accept the attendant risks. If the corporation is wholly owned, the trustee-director will apparently be safe in taking the action that is immediately most profitable to the trust beneficiary although technically it is not in the best interest of the corporation. But if the corporation is not wholly owned by the trust, it is not possible to state categorically what conduct will protect the trustee. If the will includes instructions as to corporate action, the trustee-director who follows them has the support of all present authority, but he could still have reason for not feeling entirely comfortable. If the fiduciary can get the court to advise as to the proper course of action, he will be protected, but the right to such advice is not yet entirely clear. Beyond this the trail-markers are still dim and do not present the desired path of certainty. It is to be hoped that the courts in dealing with estate corporations will realize the utility of these entities and make every attempt to harmonize the areas of conflict and provide needed stability for an area of uncertainty.

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68 See Cahn, "Estate Corporations," 86 UNIV. PA. L. REV. 136 (1937); 27 VA. L. REV. 497 (1941).