Special Provisions in a Will or Trust Occasioned by the Existence of a Business Interest

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When we come to draw the will or a trust instrument for the owner of a business, there may be a number of special provisions to be included in the document relating to the administration or disposition of that business interest. It will be possible here to consider only some of those provisions of general application. A number of the more important provisions relate to the need for expansion of the executor's or trustee's discretion in the face of the strict fiduciary duties otherwise imposed upon him by state law. For the purposes of this article Ohio law will be considered as representative.

Provision for Expediting Distribution by Executor of Stock in a Business Which Involves Substantial Risk

Under Ohio law, the executor has statutory authority to retain property as received by him, "provided the circumstances are not such as to require the fiduciary to dispose of such investment in the performance of his duties."1 If the family business is one involving substantial risks, however, the executor may not feel justified in retaining such a business interest in the estate for any length of time. The Ohio statutes do provide a method whereby property can be distributed by the executor quickly. Property which is specifically bequeathed may be delivered by the executor immediately, provided that the legatee gives security for re-delivery of the distributed property to the executor on demand.2 Thus, in the appropriate case consideration should be given to leaving the business interest as a specific legacy. A second advantage obtained by the use of a specific legacy to dispose of a business interest, where the interest is to be distributed by the executor as soon as possible, is that payment of a specific legacy, unlike payment of a general legacy, will not be deemed a distribution of income of the estate.3

3. Int. Rev. Code of 1954, § 663(a) (1) [hereinafter cited as Code §].
Provisions Authorizing Fiduciary to Loan Estate or Trust Funds to Business and to Buy and Sell Stock

Frequently, particularly if the business is a corporation, it will be planned to retain stock of the corporation in a family trust or trusts. Where that is the case, it may be important that funds of the trusts, and of estates of the family members, be available to be invested in or loaned to the business. Thus, in drafting the wills and trust agreements, the attorney should consider the advisability of giving the executor and any trustee broad authority to invest the funds of the estate or trust without restriction, and free from any requirement of diversification. 4

If it is contemplated that any person serving as a fiduciary might be a purchaser from or a seller to the estate, express authority for such dealings must be spelled out. 5

Provisions Respecting Voting of Shares

If stock of the family corporation is to be held in a trust, and perhaps during such time as it might be held in an estate as well, it will in some cases be desirable to have specific provisions in the trust document or will respecting the voting of the shares. Absent such provisions, the trustees or executors, in discharging their fiduciary responsibilities, might be unwilling to countenance the policies and incur the business risks which the family wishes to assume. This problem does not arise if the stock is non-voting stock. If it is voting stock, however, consideration should be given in drafting the documents to include specific provisions respecting voting. Co-fiduciaries might be appointed, giving one exclusive authority respecting the stock, and exculpating the other from any liability relating thereto. Or, the fiduciary might, under the terms of the instrument, be required to act respecting the stock as directed by a named person who is not a co-fiduciary, or to give a proxy to such a person, the fiduciary being exculpated from any liability in connection therewith. 6

5. OHIO REV. CODE § 2109.44. This section states that fiduciaries shall not have any dealings with the estate except as expressly authorized in the instrument creating the fiduciary relationship.
6. In drafting an irrevocable inter vivos trust, however, care must be taken respecting such voting powers, to avoid income tax danger to the grantor. Code section 675 treats the grantors as owners of stock if one not in a fiduciary capacity can direct the voting of stock without the approval or consent of one in a fiduciary capacity.

There are also possible estate tax dangers to the grantor’s estate. See State St. Trust Co. v. United States, 263 F.2d 635 (1st Cir. 1959), where the court of appeals held that if a settlor designates himself as co-trustee and retains the power to name beneficiaries, the trust is a revocable transfer causing the corpus to be included in the estate of the settlor.
Provision for Option to Purchase From the Trust or Estate

Where there may be a business interest in the estate or the trust, consideration should be given to whether anyone should have a right or option to purchase the interest or any part of it from the estate or trust. If so, a number of questions must be resolved and provisions spelled out in the documents. Is the purchase right to be an option to buy, or only a right of first refusal in the event the fiduciary proposes to sell, distribute, or otherwise dispose of the equity? How is the right to be exercised? How is the price to be arrived at? If payment is not to be all in cash, what shall be the terms of payment, and the collateral, if any? These questions should all be covered.

If a right is granted by will to purchase property from the estate for less than its fair market value, it should be recognized that the purchase price will not control the value of the property for estate tax purposes. The property will be valued in the decedent's estate at its fair market value. On the other hand, one who purchases under such an option is deemed to have acquired the property by purchase, not by inheritance or by gift, and his basis will be his cost.

Provision Authorizing Executor to Exercise Stock Option

There are many other potential problems relating to family business interests, which can be resolved by proper planning and drafting, and which are peculiar to particular assets. For example, the family head may own a stock option, which may or may not be exercised during his lifetime. If it remains unexercised at his death, will the executor have authority to exercise the option? Absent express authorization in the will, the executor's right to exercise will depend upon whether he has authority to make any investments at all, and whether he has authority to make this particular purchase having regard to the fact that it may represent a large investment in the stock of a single corporation. Thus, if it is intended that the executor have authority to exercise the stock option, that authority should be spelled out in the will. In addition, if it is intended that he have authority to borrow money, if necessary, in order to be able to pay the option price, that power too should be spelled out.

Provision Authorizing Fiduciary to Elect Under Subchapter S

If the family head owns stock in a corporation which has filed the election under Subchapter S of the Internal Revenue Code of 1954 not

7. See Ohio Rev. Code § 2109.44.
to be taxed as a corporation, such stock likewise requires special attention. On the stockholder's death his executor will become a new shareholder in the corporation, and the Subchapter S election will terminate unless the executor consents to the Subchapter S election.\footnote{11} If the executor does consent, then the estate will incur income tax on its share of the corporation's undistributed taxable income for the year,\footnote{12} which may place a burdensome cash requirement upon the estate. The executor may be reluctant to incur such an income tax liability voluntarily, without specific authorization. Accordingly, the will should include a specific authorization for the executor to file the consent under Subchapter S.

**CONCLUSION**

In a similar fashion, each business asset or interest which may be involved in the estate or a trust should be examined when the will or trust is being drafted, in the light of the intended disposition of the property and the problems which might arise in connection with the administration of the property in the estate or trust. Any specific provisions which will facilitate the intended administration and disposition of the business asset or interest should be included in the will or trust document.

\footnote{11} **CODE** § 1372. The Regulations require that the executor's election be filed within thirty days from the date he qualifies as a fiduciary, except that the thirty-day period shall in no event begin later than thirty days following the close of the corporation's taxable year in which the estate became a shareholder. **Reg.** § 1.1372-3(b) (1959).

\footnote{12} **CODE** § 1373.