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Insights

Putting the PURPOSE in a Trust: Using a Purpose Trust in a Business Succession Plan

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On September 15, 2022, Yvon Chouinard, the founder of the outdoor clothing retailer Patagonia, transferred all his voting stock of the company to a "purpose trust" and his non-voting stock to a private foundation to support environmental causes. Mr. Chouinard's recent gifts have sparked renewed interest among business owners about how to achieve business succession objectives while supporting charitable endeavors. The "purpose trust" should be in an estate planner's "toolkit" and considered in a client's business succession and charitable planning.

Purpose trusts are nothing new. They are specifically referred to in Section 409 of the Uniform Trust Act, which has been adopted in most states, including Indiana (see, Ind. Code § 30-4-2-19). A purpose trust is a non-charitable trust that is established and operates for the benefit of a "purpose" rather than a specific "person." Most commonly, the "purposes" in a purpose trust have been designed for caring for a pet, a family homestead, or cemetery plots. However, business owners are now using purpose trusts for values-aligned, business ownership and succession. The "purpose" becomes the enabling of the continuation of the company's mission, values, and manner of operation. For some, the purpose may focus on providing benefit to a specific group of stakeholders/employees. For others, the purpose may focus on a larger, external vision and expand on what is possible for the future of the company. Other examples include:

- Maintaining and improving the quality of a company's offerings.
- Enshrining certain practices that relate to the company's commitment to the environment, community, or other stakeholders.
- Promoting a way of doing business such as creating high quality jobs or value-driven hiring and sourcing processes.
- Ensuring the company leadership never misuses its economic power to contribute to causes that directly oppose the values set forth by the founders.

No matter the purpose, it should be clearly stated in the trust instrument and bolstered by objectives, also stated in the trust instrument. The purpose and objectives create a roadmap for the key positions involved with a purpose trust, those being the trust stewardship committee, trustee, and trust enforcer, but also for the actual operators of the company.

A purpose trust is generally a "directed trust" with the trustee holding the assets and acting on behalf of the trust; however, those actions are directed by a trust stewardship committee. That committee, then, maintains

the duty of ensuring the purpose of the trust is upheld. Generally, that committee is comprised of a broad range of stakeholders, including employees, key customers, investors, and community representatives. The specific roles and responsibilities of the committee also need to be clearly stated in the trust instrument and include such things as investment decisions related to the trust assets, distribution approval, limited modification of the trust instrument (only as necessary), as well as electing a Board of Directors for the company, and appointing or removing the trustee or trust enforcer. Importantly, normal business operations of the company still require separate management (i.e. officers and board of directors) but that management is now held accountable by the committee and trustee as the voting shareholder of the company.

The trustee will be responsible for the prudent management of the trust in accordance with the trust instrument and its purpose. The trustee is also responsible for the trust's general administration, including tax reporting and record keeping. Generally, outside of some administrative tasks, the trustee will have no substantial role in decision making and will not be overly-involved in the running of the company unless directed by the committee. Often, a trustee will be selected depending on where such trustee is physically located in order to domicile the purpose trust in a specific state and take advantage of that state's laws with respect to such things as state-level taxation and perpetuity rules.

The trust enforcer serves as a de facto "beneficiary" since the trust does not have any readily identifiable beneficiaries. A trust enforcer is responsible for enforcing the purpose and ensuring the committee and trustee operate the trust in the interest of that founding purpose. A trust enforcer may request and review information on assets held by the trust, financial documents related to the company, and address grievances from stakeholders and even pursue legal action to enforce the purposes of the trust.

All these positions work within a system of checks and balances to ensure the purpose of the trust is followed. To maintain this system, governance issues should be addressed in the trust instrument as well, such as number of members/positions, how decisions are made by a committee/trustee/enforcer, how often meetings occur, term limits, and removal and successor appointment procedures for the various positions. Additional positions can also be included to further divide authority.

Ultimately, the purpose trust is a potentially powerful strategy for business owners who want to continue the company's mission and values or even embark on a "higher purpose." In a world where most business owners know about selling their company, taking their company public, donating their stock to charity, or implementing employee stock ownership plans, the purpose trust is an alternative tool that may allow business owners to "have their cake and eat it too," ensuring the continuity of their for-profit business but also providing for the welfare of their employees while achieving charitable objectives. As practitioners, there are rewarding opportunities to advise and support business owner clients who are interested in leaving a lasting legacy.

If you have questions regarding information found in this alert, please contact **Micah J. Nichols** or **Rodney S. Retzner**.

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