

Clarifying the Business Trust in Bankruptcy: A Proposed Restatement Test

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I. INTRODUCTION

When bankruptcy courts attempt to define the business trust, “[t]he decisions are sharply, and perhaps hopelessly, divided.”¹ The Bankruptcy Code, which guides the determinations of bankruptcy courts, specifically lists business trusts as eligible for protection.² However, the Code does not define what a business trust is and does not list any criteria for determining when a trust is a business trust.³ The lack of a concrete definition has led many courts

1. *In re Medallion Realty Tr.*, 103 B.R. 8, 10–11 (Bankr. D. Mass. 1989), *aff’d*, 120 B.R. 245 (D. Mass. 1990); *see also infra* Part III.

2. *See* 11 U.S.C. § 109(b) (2012); *see also infra* Part III.

3. *See* 11 U.S.C. § 109(b) (listing the business trust as eligible for protection under corporate eligibility but supplying no further information).

to formulate their own definitions of business trusts.⁴ While the courts hoped that they would eventually settle on a uniform test to tackle this issue, it has yet to occur.⁵ Presently, courts apply varying tests, some of which propose twenty-four individual factors to consider while others adopt tax and state laws.⁶ This confusion regarding the appropriate test leads to uncertainty on behalf of debtors, who are unsure if they will be eligible for bankruptcy protection.⁷

The history of the business trust dates back to the early thirteenth century.⁸ Since that time, the business trust has evolved considerably.⁹ However, certain characteristics of the business trust have remained constant throughout its history.¹⁰ First, the business trust was initially a tool to circumvent strict incorporation statutes that restricted the creation of corporations.¹¹ Citizens seeking the benefits of a corporate structure were forced to create voluntary associations, such as business trusts, to avoid strict government oversight.¹² Second, business trusts allow the trustee more power over the trust property than the officers of a corporation have over a corporation.¹³ In addition, unlike a corporation, the trustees are the “masters” of the business trust.¹⁴ This structure leads to a unique relationship between the beneficiaries and the trustee of the business trust.¹⁵ Third, business trusts allow for the limited liability of the trustee, who is only liable in her fiduciary capacity.¹⁶ All of these aspects evolved into the structure of the business trust and should remain relevant in its treatment by the courts.¹⁷

In order to cure the confusion that has resulted from the absence of a clear definition of the business trust in bankruptcy, a single uniform test should be

4. See *infra* Part III (describing the various tests that the courts apply, ranging from a twenty-four-point test to an income tax law analysis).

5. See *infra* Part III.

6. See *Morrissey v. Comm’r*, 296 U.S. 344 (1935) (applying a test based on federal income tax law); *In re Cohen*, 4 B.R. 201, 203 (Bankr. S.D. Fla. 1980) (applying a twenty-four-point test); *infra* Part III.

7. See *infra* Part III.

8. See *infra* Part II.

9. See *infra* Part II.

10. See *infra* Part II.

11. See *infra* Part II.

12. See *infra* Part II.

13. See *infra* Part II; see also *Williams v. Inhabitants of Milton*, 102 N.E. 355, 358 (Mass. 1913) (setting forth the “masters” of the trust analysis).

14. See *Williams*, 102 N.E. at 358.

15. See *infra* Part II.

16. See *infra* Part II; see also *Larson v. Sylvester*, 185 N.E. 44, 45–46 (Mass. 1933).

17. See *infra* Part IV.B.

enacted.¹⁸ This Comment proposes a restatement test that incorporates the history of the business trust as well as courts' various approaches into a single uniform test.¹⁹ This test will reduce debtors' uncertainty by creating a consistent approach to determine when a trust is a business trust.²⁰

Part II of this Comment will address the history of the business trust from its roots in feudal England to its use as a tool to circumvent strict corporate statutes.²¹ Part III will outline the current state of the law regarding business trusts, both within and outside the bankruptcy context.²² Part IV proposes a four-factor test to remedy the courts' current confusion regarding business trusts.²³

II. HISTORY OF THE BUSINESS TRUST

The trust has roots leading back to Franciscan friars in thirteenth century England.²⁴ The friars were unable to own property, so landowners conveyed property to friends of the friars to hold for their use and benefit.²⁵ Not long thereafter, landowners used the early trust organization as a way to circumvent the primogeniture rules in place at the time.²⁶ The business trust, however, developed later and shares roots with corporations found in eighteenth-century England.²⁷ At that time, corporations in England required authorization by an

18. *See infra* Part IV.B.1–4.

19. *See infra* Part IV.B.1–4.

20. *See infra* Part IV.B.

21. *See infra* Part II.

22. *See infra* Part III.

23. *See infra* Part IV.

24. JESSE DUKEMINIER & ROBERT H. SITKOFF, *WILLS, TRUSTS, AND ESTATES* 386 (9th ed. 2013) (providing a concise description of the evolution of the trust and later describing the current treatment of the trust by the courts).

25. *Id.* (“O, owner of Blackacre, would *enfeoff* A and his heirs to hold Blackacre *to the use of* the friars. By this transfer, the legal fee simple passed from O, the *feoffor to uses*, to A, the *feoffee to uses* who held it for the benefit” of the friars).

26. *Id.*; *see also* *Primogeniture Definition*, ENCYCLOPEDIA.COM (2003), <http://www.encyclopedia.com/topic/primogeniture.aspx> (“Primogeniture has two closely related meanings: (1) a principle of seniority and authority whereby siblings are ranked according to their ages, with the eldest coming first; and (2) a principle of inheritance, in which the firstborn child receives all or his parents' most significant and valuable property upon their death.”). In application, the primogeniture rules of the time led to the disinheritance of younger siblings and females from their father's estate. *See Primogeniture*, PRINCETON U., <https://www.princeton.edu/~achaney/tmve/wiki100k/docs/Primogeniture.html> (last visited Mar. 5, 2016). Typically, the first-born son inherited the entire estate and would then be responsible for passing any inheritance to his siblings. *Id.*

27. EDWARD H. WARREN, *CORPORATE ADVANTAGES WITHOUT INCORPORATION: AN*

act of Parliament or a charter from the Crown.²⁸ The process of obtaining authorization from the Crown or Parliament was rigorous, and many citizens formed voluntary associations to offer shares to the public without this proper authorization.²⁹ In order to stop this practice, British Parliament passed the English Bubble Act in 1719 to limit the creation of associations that attempted to act as corporate bodies.³⁰ British Parliament later repealed the Bubble Act in 1825; however, this early history serves to point out the genesis of voluntary associations other than corporations.³¹

Later, in 1860, citizens created another type of voluntary association in Great Britain: the investment trust.³² Investment trusts were professionally managed associations that “held diversified assets to reduce investors’ risks.”³³ Again, this type of trust structure did not last long.³⁴ Parliament enacted the Companies Act in 1862, which required these trusts to register under the title of company but allowed them to keep their preexisting structure.³⁵ Early in its history, British Parliament enacted several obstacles in the way of business

EXAMINATION OF THE LAW RELATING TO ORDINARY PARTNERSHIPS, LIMITED PARTNERSHIPS, PARTNERSHIP ASSOCIATIONS, JOINT-STOCK COMPANIES, BUSINESS TRUSTS, UNINCORPORATED LABOR UNIONS, AND DE FACTO CORPORATIONS FOR THE PURPOSE OF ASCERTAINING UNDER WHAT, IF ANY, CIRCUMSTANCES THERE MAY BE CORPORATE ADVANTAGES WITHOUT INCORPORATION 330 (1929).

28. *See id.*

29. Sheldon A. Jones, *The Massachusetts Business Trust and Registered Investment Companies*, 13 DEL. J. CORP. L. 421, 425 (1988); *see also* TAX COMM’R’S DEP’T, REPORT OF THE TAX COMMISSIONER UPON VOLUNTARY ASSOCIATIONS, H.R. REP. NO. 1646, at 2 (Mass. 1912), <https://play.google.com/books/reader?id=7pssAAAAYAAJ&printsec=frontcover&output=reader&hl=en&pg=GBS.PA1> (defining a voluntary association as “an association of persons with a combined capital, represented by transferable shares, for the purpose of carrying on a common project for gain.”).

30. WARREN, *supra* note 27, at 330 (noting that the Bubble Act sought to eliminate any association which “presumed to act as if they were corporate bodies, and have pretended to make their shares in stocks transferable or assignable, without any legal authority, either by act of Parliament, or by a charter from the Crown”).

31. *Id.* at 331.

32. *See* AVARD L. BISHOP & LELAND R. ROBINSON, INVESTMENT TRUST ORGANIZATION AND MANAGEMENT 187–207 (1926); THEODORE J. GRAYSON, INVESTMENT TRUSTS, THEIR ORIGIN, DEVELOPMENT AND OPERATION 1 (1928).

33. Jones, *supra* note 29, at 425; *see also* DUKEMINIER & SITKOFF, *supra* note 24, at 398–99 (stating that modernly the investment trust structure is commonly relied on in mutual funds and is commonly used in asset securitization and employee trust funds).

34. Jones, *supra* note 29, at 425.

35. *See* David Kershaw, *The Path of Corporate Fiduciary Law*, 8 N.Y.U. J.L. & BUS. 395, 418 n.86 (2012) (“*See e.g.*, Companies Act, 1862, 25 & 26 Vict., c. 89, § 6 (“Any seven or more persons associated for any lawful purpose may, by subscribing their names to a Memorandum of Association . . . form an incorporated company, with or without unlimited liability.”) (footnotes omitted).”).

trusts.³⁶ However, the characteristic of the business trust as a tool to circumvent strict statutes remains an important facet to this day.³⁷

In the United States, Massachusetts served as the forefront of the practical and legal evolution of business trusts because it was one of the last “states to permit incorporation without [a] special legislative act.”³⁸ Such delayed legislation encouraged the creation of business trusts because, much like the system in Britain, citizens sought to circumvent the strict standards set out by the Massachusetts legislature.³⁹ The state’s corporate statute “(1) prohibited dealing in real estate; (2) established minimum and maximum capital amounts; and (3) required corporations to file detailed annual statements of assets and liabilities.”⁴⁰ Due to their flexible nature, business trusts allowed citizens to circumvent these strict standards.⁴¹ Later in the nineteenth and early twentieth centuries, Massachusetts street railway companies and electric and gas utility companies made use of business trusts to avoid these strict statutory limitations.⁴² Massachusetts business trusts allowed trustees of these companies to issue an unlimited amount of capital and allowed opportunities for more efficient management.⁴³ Additionally, the amount of flexibility achieved under a business trust led many investment companies to organize under the Massachusetts business trust structure.⁴⁴ The history of the practical evolution of the business trust is one of circumventing strict statutory

36. See *supra* notes 27–29, 35 and accompanying text.

37. See *infra* Part IV.

38. Jones, *supra* note 29, at 425–26; see also E. Merrick Dodd, *Statutory Developments in Business Corporation Law, 1886–1936*, 50 HARV. L. REV. 27, 31 (1936) (discussing early Massachusetts corporation statutes).

39. See Jones, *supra* note 29, at 426.

40. *Id.*; see also MASS. PUB. STAT. tit. XV, ch. 106, §§ 14, 54 (1882), <https://ia902604.us.archive.org/7/items/publicstatutesof00mass/publicstatutesof00mass.pdf>.

41. See JOHN H. SEARS, TRUST ESTATES AS BUSINESS COMPANIES 357–61 (2d ed. 1998). Business trusts are entities with greater “flexibility” and “continuity” of management than corporations. *Id.* Business trusts have more flexibility because trustees could “transact business with more ease and rapidity than directors” and more continuity because “trustees who are the managing officers of a trust are not so likely to be changed as are the officers of a corporation.” *Id.* at 360.

42. Jones, *supra* note 29, at 427. At the time, there was a statutory limitation on the amount of capital a corporation could issue. *Id.* There was also some “uncertainty whether a corporation could own the controlling shares of other utilities.” *Id.*

43. *Id.* See generally TAX COMM’R’S DEP’T, RESOLVE TO PROVIDE FOR AN INVESTIGATION OF VOLUNTARY ASSOCIATIONS ORGANIZED OR DOING BUSINESS IN THIS COMMONWEALTH UNDER WRITTEN INSTRUMENTS OR DECLARATIONS OR TRUST, Mass. House Rep. No. 1646, at 2 (1912).

44. SEC, INVESTMENT TRUSTS AND INVESTMENT COMPANIES, H.R. DOC. NO. 70, at 28–29 (1st Sess. 1939).

requirements.⁴⁵ Thus, it is only fitting that the definition of this evading tactic still escapes us today.⁴⁶

In addition to the practical evolution of the business trust, the legal development in Massachusetts is equally informative.⁴⁷ Late in the nineteenth century, in *Ricker v. American Loan & Trust Co.*, the Massachusetts Supreme Judicial Court tackled the issue of tax treatment of a partnership.⁴⁸ Here, the court treated the New England Car Trust as a partnership for tax purposes.⁴⁹ The purpose of the New England Car Trust was to buy, sell, and lease railroad rolling stock.⁵⁰ The court held that “[t]here is no intermediate form of organization between a corporation and a partnership Since this association is not a corporation, its members must be partners.”⁵¹ Although the court in *Ricker* did not recognize the existence of a business trust, it was one of the first times that a court dealt with a trust that did not fit neatly into the statutory definition of a corporation or partnership.⁵²

However, five years later, in *Mayo v. Moritz*, the same court held that a business trust was a separate entity from a corporation.⁵³ In *Mayo*, the defendant assigned his rights in an invention to four trustees.⁵⁴ The object of the trust was to sell shares in the trust, which gave the shareholders a stake in the invention and raised capital to fund the invention and any further research of the defendant.⁵⁵ The court held that “[t]he deed of trust does not have the effect to make the scrip-holders partners.”⁵⁶ In the opinion, the court failed to categorize the trust agreement as either a partnership or a corporation.⁵⁷ Thus,

45. See *supra* notes 29–43 and accompanying text.

46. See *infra* Part III.B.

47. See *DUKEMINIER & SITKOFF*, *supra* note 24, at 398 (“The business trust was so common in Massachusetts, where corporate ownership of real estate was prohibited, that the term *Massachusetts trust* became synonymous with business trust.”). Consequently, the case law in Massachusetts, because of the popularity of the business trust in that state, serves as a good lens through which to analyze the legal development of the business trust.

48. *Ricker v. Am. Loan & Tr. Co.*, 5 N.E. 284 (Mass. 1885).

49. *Id.* at 285.

50. *Id.*

51. *Id.* at 286.

52. See *Jones*, *supra* note 29, at 429.

53. *Mayo v. Moritz*, 24 N.E. 1083 (Mass. 1890).

54. *Id.* at 1083.

55. *Id.* The main issue of the case is partnership liability for rents, but this case serves as an initial recognition of business trusts in American jurisprudence. *Id.*; see also *Jones*, *supra* note 29, at 429.

56. *Mayo*, 24 N.E. at 1083. The court goes on to say the trustees are personally liable for their debt to the plaintiff and that creditors may only seek damages from the trust fund. *Id.*

57. *Id.*

unlike the previous decisions where the Massachusetts courts spent a considerable amount of effort defining trust arrangements as either a corporation or partnership, the court in *Mayo* spent little time on the question.⁵⁸ In fact, the court did not even attempt to label the trust, thereby allowing the trust arrangement to occupy a gray area in the law between a corporation and a partnership.⁵⁹

While the *Mayo* court did not specifically call the trust a business trust, it did not attempt to fit the organization into either a partnership or corporation as the court did in *Ricker*.⁶⁰ *Mayo* is the first case in Massachusetts to carve out a gray area for a trust that does not meet the standards of a corporation or partnership, paving the way for the recognition of the business trust in the future.⁶¹ Unfortunately, there is no policy discussion in either *Ricker* or *Mayo* to shed some light on the reason for this change in analysis.⁶²

The first time the Supreme Judicial Court of Massachusetts specifically recognized a trust as a separate entity was in *Williams v. Inhabitants of Milton*.⁶³ In *Williams*, the court addressed the issue of whether a Boston realty trust should be treated as a trust or partnership for tax purposes.⁶⁴ In the declaration of trust, the trustee had the power to: “(1) issue transferable shares of beneficial interest in the trust; (2) hold the trust funds and property for the benefit of shareholders; (3) invest the trust funds in real estate, including bonds and notes on real estate; (4) improve and lease real estate; and (5) borrow money.”⁶⁵ Additionally, the trust’s shareholders had rights similar to those of stockholders—they could receive income from their share in the trust and receive their share of the trust if or when the trust was terminated.⁶⁶ *Williams* is distinct from *Ricker* because the organization of the trust in *Williams* was such that the trustees controlled the property and they were the “masters” of the trust.⁶⁷ In *Ricker*, however, there was “no association between the certificate

58. Compare *id.*, with *Ricker v. Am. Loan & Tr. Co.*, 5 N.E. 284 (Mass. 1885).

59. See *Mayo*, 24 N.E. at 1083.

60. Compare *id.*, with *Ricker*, 5 N.E. at 284.

61. *Mayo*, 24 N.E. at 1083.

62. See *Mayo*, 24 N.E. at 1083; *Ricker*, 5 N.E. at 284–88.

63. 102 N.E. 355 (Mass. 1913).

64. *Id.* at 356.

65. Jones, *supra* note 29, at 430; see also *Williams*, 102 N.E. at 356 (declaration of trust language is included in state reporter only).

66. *Williams*, 102 N.E. at 356.

67. *Id.* at 357.

holders” and the trustees.⁶⁸ Additionally, the *Williams* court relied on an English case that had similar facts and found the organization in question there was a trust and not a partnership to support its finding.⁶⁹ However, in the court’s eyes, the most dispositive factor showing that the organization was a trust was that the trustees were the “masters” of the property.⁷⁰

In 1933, the court in *Larson v. Sylvester* recognized the business trust as a separate entity.⁷¹ This case confronted the issue of liability for debts in a corporation versus a partnership.⁷² The court determined that the trust was conducting business because the trust issued transferable shares, which was sufficient to create a business trust at the time.⁷³ Additionally, the court found that a “trust is not a legal personality” and cannot be sued, unlike a corporation.⁷⁴ In this case, the trustee was acting for the benefit of the shareholders and was liable only in his fiduciary capacity; the trust itself was not liable.⁷⁵ Such separation of liability between the trust and the trustee is an important characteristic of the business trust and should play a major role in the way modern courts define the business trust.⁷⁶ Additionally, many states recognize the distinction between the business trust and other entities for tax purposes.⁷⁷ A relevant Minnesota statute provides that a business trust shall be

68. *Id.* (finding that the organization of the trust in *Ricker* lent itself to treatment as a partnership); see also *Ricker v. Am. Loan & Tr. Co.*, 5 N.E. 284 (Mass. 1885).

69. *Williams*, 102 N.E. at 358; *Smith v Anderson* (1880) 15 App. Cas. 247 (PC) (appeal taken from Austl.).

70. *Williams*, 102 N.E. at 358. The court undertakes a thorough discussion of case precedent and examines the relationships between beneficiaries and their trustees. *Id.* at 356–59. The court eventually concludes that the main factor in determining whether an organization is a trust is whether the trustees are the “masters” of the trust property as opposed to the beneficiaries having control over the trust property. *Id.* at 358–59.

71. 185 N.E. 44, 46 (Mass. 1933).

72. *Id.* at 45.

73. *Id.*

74. *Id.*

75. *Id.*

76. See *infra* Part IV (discussing the proposed test, which seeks to incorporate the history of the business trust as well as the previous opinions of the courts).

77. ALA. CODE §§ 19-3-60 to -67 (1975); ARIZ. REV. STAT. ANN. §§ 10-501 to -509 (1987); FLA. STAT. § 609.01–08 (1994); IND. CODE §§ 23-5-1 to -11 (1987); KAN. STAT. ANN. §§ 17-2027 to -2038 (1987); KY. REV. STAT. ANN. §§ 386.370–440 (West 1987); MINN. STAT. §§ 318.01–06 (2015); MISS. CODE ANN. §§ 79-15-1 to -29 (1987); MONT. CODE ANN. §§ 35-5-101 to -205 (1987); N.Y. GENERAL ASS’NS LAW § 1-21 (McKinney 1987); N.C. GEN. STAT. §§ 39-44 to -47 (1987); OHIO REV. CODE ANN. §§ 1746.01–99 (West 1987); OR. REV. STAT. §§ 128.560–.595 (1987); S.C. CODE ANN. §§ 33-53-10 to -50 (1987); S.D. CODIFIED LAWS §§ 47-14-1 to -13 (1987); TENN. CODE ANN. § 48-14-101 (1987); WASH. REV. CODE §§ 23.90.010–040 (1987); W. VA. CODE §§ 47-9A-1 to -6; WIS. STAT. § 226.14 (1987).

a “separate unincorporated association, not a partnership, joint stock association, agency or any other relation except a business trust.”⁷⁸ To conclude, separation and circumvention were the driving forces behind the formation and recognition of the business trust, and this foundation should remain relevant in the modern treatment of the business trust by bankruptcy courts.⁷⁹

III. CURRENT STATE OF THE LAW

A. *Outside the Bankruptcy Context*

Generally, the business trust is grouped under the umbrella of commercial trusts as opposed to gratuitous trusts.⁸⁰ Often when someone thinks of a trust, the gratuitous trust comes to mind.⁸¹ In a gratuitous trust, an individual (the settlor) leaves property in trust to a trustee to hold for the benefit of beneficiaries.⁸² The primary difference between a gratuitous trust and a commercial trust “is that the settlor in a gratuitous trust receives no compensation for the conveyance whereas the settlor in a commercial trust—typically a corporation or financial institution—always receives payment for the assets conveyed to the trust.”⁸³ There are two types of trusts under the commercial trust umbrella: the traditional commercial trust and the business trust.⁸⁴ The traditional commercial trust operates more like a gratuitous trust in that the first goal of the traditional commercial trust “is to collect, to preserve,

78. MINN. STAT. § 318.02(2). The subdivision provides:

[A]ny such association heretofore or hereafter organized shall be a business trust and a separate unincorporated association, not a partnership, joint-stock association, agency, or any other relation except a business trust. A business trust is also known as a common law trust and Massachusetts trust for doing business.

Id.

79. *See infra* Part IV (discussing the proposed test, which seeks to incorporate the history of the business trust as well as the previous opinions of the courts).

80. *See* Thomas E. Plank, *The Bankruptcy Trust as a Legal Person*, 35 WAKE FOREST L. REV. 251, 255 (2000). The main areas of focus for study in the trust context regard family wealth transfers or donative trusts. *Id.* However, it has been estimated that over ninety-nine percent of the wealth that is held in trust in the United States is held in commercial trusts. *See* John H. Langbein, *The Contractarian Basis of the Law of Trusts*, 105 YALE L.J. 625, 632–33 (1995).

81. *See* Langbein, *supra* note 80, at 632.

82. *See id.*

83. Steven L. Schwarcz, *Commercial Trusts as Business Organizations: Unraveling the Mystery*, 58 BUS. LAW. 559, 562 (2003).

84. *See* Plank, *supra* note 80, at 256.

and to distribute the trust estate.”⁸⁵

While the business trust is similar in many ways to its counterpart, the traditional commercial trust, it has several distinctions.⁸⁶ Most generally, the goal of the business trust is not to preserve the trust property but rather to use the property to conduct business and make a profit.⁸⁷ In addition to the typical trust agreement, the business trust agreement “not only prescribes the assets of the trust, the duties and responsibilities of the trustee, and the rights of the beneficiaries; it also prescribes the permissible business activities of the trust.”⁸⁸ Common examples of the unlimited business capabilities of the business trust include mutual funds organized as trusts,⁸⁹ real estate investment trusts where the trustee actively manages property,⁹⁰ and business trusts that issue “debt to acquire financial assets on a revolving basis.”⁹¹

Structurally, the business trust is designed to be similar to a corporation and “is considered a legal person in many contexts.”⁹² Such structure dictates that the business trust exists apart from the people who created and comprise it.⁹³ This separation and personhood allows a business trust to be a debtor in

85. *Id.*; see also RESTATEMENT (SECOND) OF TRUSTS §§ 169, 172–73, 175–82, 227 (AM. LAW INST. 1959). Other characteristics of the traditional commercial trust include: the appointment of a trustee by the beneficiaries of the trust; the power of the trustee to act on behalf of the beneficiaries, which includes suing and defending suits; and that the trustee does not have the broad power to conduct business activities. *Id.*

86. See Plank, *supra* note 80, at 258 (“In a business trust, as in a traditional trust, property is conveyed pursuant to a trust agreement to one or more trustees for the benefit of a defined group of beneficiaries.”).

87. See GEORGE BOGERT ET AL., THE LAW OF TRUSTS AND TRUSTEES: A TREATISE COVERING THE LAW RELATING TO TRUSTS AND ALLIED SUBJECTS AFFECTING TRUST CREATION AND ADMINISTRATION WITH FORMS §§ 2–7 (1984) (describing the means employed by a trustee in using the trust property to operate a business).

88. See Plank, *supra* note 80, at 258.

89. See Northstar Fin. Advisors, Inc. v. Schwab Invs., 807 F. Supp. 2d 871, 877 (N.D. Cal. 2011).

90. See, e.g., Lafayette Bank & Tr. Co. v. Branchini & Sons Constr. Co., 342 A.2d 916, 917 (Conn. Super. Ct. 1975) (discussing a real estate investment trust organized under Maryland law).

91. See Plank, *supra* note 80, at 259; see also Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd., 116 F.3d 790, 794 (5th Cir. 1997) (involving a business trust issuer of \$87,000,000 worth of bonds secured by mortgage loans refinancing six hotels). Some scholars estimate that the amount held in securitization trusts could be in the trillions. See Schwarcz, *supra* note 83, at 559.

92. Plank, *supra* note 80, at 260; see, e.g., CONN. GEN. STAT. § 34-501(2) (2012) (providing that a statutory trust, which includes a business trust, shall be “a separate legal entity”); DEL. CODE ANN. tit. 12, § 3801(g) (2016) [hereinafter Delaware Trust Act] (providing that a trust shall be “a separate legal entity”); MINN. STAT. § 318.02 (2015) (providing that an association organized under the statute “shall be a business trust and a separate unincorporated legal entity”).

93. See Plank, *supra* note 80.

bankruptcy.⁹⁴

Outside of the bankruptcy context, the definitions associated with the business trust vary greatly depending on the state's laws.⁹⁵ The foremost statute regarding business trusts is the Delaware Statutory Trust Act of 1988.⁹⁶ The Delaware Statutory Trust Act requires that a business trust hold, manage, invest, or perform business or professional activities for profit.⁹⁷ However, when looking at the whole, outside of the bankruptcy context, there are four general requirements in order to consider a trust a business trust: (1) there must be a trustee; (2) the trustee controls identifiable property; (3) the trust must engage in business; and (4) the trust must issue transferable shares.⁹⁸ The

94. Only a "person" or a municipality may be a debtor under the Code. See 11 U.S.C. §§ 101(13), 109(a) (2012). "Person" includes an individual, partnership, corporation, and, in certain limited instances, a governmental unit. See *id.* § 101(41). A corporation includes a "business trust." See *id.* § 101(9)(A)(v); see also *Rainbow Tr., Bus. Tr. v. Moulton Constr. Co. (In re Rainbow Tr., Bus. Tr.)*, 207 B.R. 70, 72–73 (Bankr. D. Vt. 1997) (business trust; Chapter 11), *aff'd sub nom.* Official Unsecured Creditors' Comm. of the Rainbow Tr. v. Moulton Constr. Co. (*In re Rainbow Tr.*), 216 B.R. 77 (B.A.P. 2d Cir. 1997); *Lemley–Cabbiness Farms v. Fed. Deposit Ins. Corp. (In re Lemley Estate Bus. Tr.)*, 65 B.R. 185, 188 (Bankr. N.D. Tex. 1996) (business trusts serving as general partners of a partnership operating a farm; Chapter 11); *In re Affiliated Food Stores, Inc. Grp. Benefit Tr.*, 134 B.R. 215, 217 (Bankr. N.D. Tex. 1991) (trust established to provide health benefits for employees of business and families; Chapter 11); *Carr v. Mich. Real Estate Ins. Tr. (In re Mich. Real Estate Ins. Tr.)*, 87 B.R. 447, 449 (Bankr. E.D. Mich. 1988) (insurance trust; Chapter 7); *Merrill v. Allen (In re Universal Clearing House Co.)*, 60 B.R. 985, 989–93 (Bankr. D. Utah 1986) (finding clearinghouse a business trust eligible for relief under the Code); *In re Arehart*, 52 B.R. 308, 311 (Bankr. M.D. Fla. 1985) (finding a trust for developing, operating, leasing, and selling trust property eligible).

95. See *supra* note 77 and accompanying text (listing various state's statutory definitions of bankruptcy trusts).

96. *DUKEMINIER & SITKOFF, supra* note 24, at 386; see also *DEL. CODE ANN. tit. 12, §§ 3801–63.*

97. The entire provision states:

"Statutory trust" means an unincorporated association which: Is created by a governing instrument under which property is or will be held, managed, administered, controlled, invested, reinvested and/or operated, or business or professional activities for profit are carried on or will be carried on, by a trustee or trustees or as otherwise provided in the governing instrument for the benefit of such person or persons as are or may become beneficial owners or as otherwise provided in the governing instrument, including but not limited to a trust of the type known at common law as a "business trust," or "Massachusetts trust," or a trust qualifying as a real estate investment trust under § 856 et seq. of the United States Internal Revenue Code of 1986 [26 U.S.C. § 856 et seq.], as amended, or under any successor provision, or a trust qualifying as a real estate mortgage investment conduit under § 860D of the United States Internal Revenue Code of 1986 [26 U.S.C. § 860D], as amended, or under any successor provision; and (2) Files a certificate of trust pursuant to § 3810 of this title.

DEL. CODE ANN. tit. 12, § 3801(g)(1)–(2).

98. See *Plank, supra* note 80, at 263. *Black's Law Dictionary* defines the business trust as "[a] form of business organization, similar to a corporation, in which investors receive transferable certificates of

courts generally do not discuss whether the trust has identifiable property and a trustee; however, much of the discussion about the definition of a business trust relates to the issue of what a trust engaged in business looks like.⁹⁹

It may seem like the business trust is simply a corporation taking an alternative form, but there are distinctions between the two.¹⁰⁰ A corporation is a legal entity that acts through its agent, while the trust can do no act itself.¹⁰¹ In a trust, it is the trustee alone who can act in the interest of the beneficiaries.¹⁰² Thus, the trustee is liable in his fiduciary capacity if anything goes wrong and the trust itself is not liable.¹⁰³ Another distinction is that beneficiaries of the trust, even if they hold transferable shares in the trust, do not have the right to instruct the trustee how to manage the trust.¹⁰⁴ This is very different from the world of corporations where shareholders can have a massive effect on the activities of the corporation.¹⁰⁵ Additionally, there are several advantages to the business trust over corporations, including the ability of the trustee to terminate the trust without shareholder approval.¹⁰⁶ Overall, the

beneficial interest instead of stock shares.” *Trust*, BLACK’S LAW DICTIONARY (10th ed. 2014).

99. See *infra* Part III.B.2.

100. *Dolben v. Gleason*, 198 N.E. 762, 763 (Mass. 1935).

101. *Id.*

102. *Id.* at 763–64.

103. *Id.*; see also *Larson v. Sylvester*, 185 N.E. 44, 46 (Mass. 1933).

104. *Williams v. Inhabitants of Milton*, 102 N.E. 355, 357 (Mass. 1913) (finding that the trustees were the “masters” of the trust).

105. Stuart L. Gillan & Laura T. Starks, *Corporate Governance Proposals and Shareholder Activism: The Role of Institutional Investors*, 57 J. FIN. ECON. 275, 275 (2000). Shareholders are often referred to as the owners of the company and can have a considerable effect on the way the company is run. See Kathy Zheng, *How Shareholders Affect a Business*, AZ. REPUBLIC, <http://yourbusiness.azcentral.com/shareholders-affect-business-8879.html> (last visited Mar. 6, 2016). Shareholders can affect the business through their right to vote in company decisions. *Id.* Generally, this voting right is equal to the amount of shares they own; while other structures are available, one share usually equals one vote. *Id.* The shareholders can vote to establish the board as well as elect new board members. *Id.* The shareholders also have the right to approve or disallow major mergers or acquisitions. *Id.*; see also Shaun Hoyes, *To What Extent Do Shareholders Control the Activities of a Corporation?*, AZ. REPUBLIC, <http://yourbusiness.azcentral.com/extent-shareholders-control-activities-corporation-27955.html> (last visited Mar. 6, 2016).

106. Other benefits include:

The declaration of trust may provide that (i) no share certificates will be issued; . . . (iii) the trustees may effect a ‘reverse split’ of outstanding shares; (iv) notice of shareholders’ meetings need not be given to certain shareholders whose mail is habitually returned, consistent with the SEC’s proxy rules; (v) the shareholder vote required to approve an action such as a consolidation, the sale of assets, or an amendment to the declaration of trust can be less than required by state corporate law or can be eliminated; and (vi) the trustees may change the name of the trust or a series without shareholder approval.

Sheldon A. Jones, Laura M. Moret & James M. Storey, *The Massachusetts Business Trust and*

business trust can provide an alternative to creating a corporation and is a beneficial instrument for many companies.¹⁰⁷

B. Inside the Bankruptcy Context

1. A Brief Bankruptcy Introduction

United States bankruptcy law has its roots in Article I, Section 8 of the Constitution, which authorizes Congress to enact “uniform Laws on the subject of Bankruptcies.”¹⁰⁸ Using this power, Congress enacted the Bankruptcy Code in 1978, which is codified under Title 11 of the United States Code and serves as the uniform law governing bankruptcy.¹⁰⁹ The fundamental goal of the Bankruptcy Code is to allow debtors to discharge debts and have a financial fresh start while paying off as much debt as possible to their creditors.¹¹⁰ There are six separate types of bankruptcy cases: Chapters 7, 9, 11, 12, 13, and 15, all given the names of the chapters of the Bankruptcy Code that describe them.¹¹¹ Chapter 7 is used when the debtor seeks to liquidate assets to pay the debts he or she can.¹¹² Chapter 9 is primarily for the use of a municipality and allows that entity to reorganize its debts to pay creditors.¹¹³ Chapter 11 provides an individual or corporate debtor the opportunity to reorganize their debts.¹¹⁴ This Chapter allows the debtor, usually a business, to remain in operation and provide a plan to pay off some debts and discharge others.¹¹⁵ Chapter 12 is rarely used and provides specific protections for family farmers and fishermen.¹¹⁶ Chapter 13 is similar to Chapter 11 in that the debtor must

Registered Investment Companies, 13 DEL. J. CORP. L. 421, 458 (1988).

107. *See supra* notes 105–06 and accompanying text.

108. U.S. CONST. art. I, § 8.

109. *See generally* BANKR. JUDGES DIV., ADMIN. OFFICE OF THE U.S. COURTS, BANKRUPTCY BASICS (3d. ed. 2011), <http://www.uscourts.gov/uscourts/FederalCourts/BankruptcyResources/bankbasics.pdf> (providing an introduction to the practices of the bankruptcy courts as well as the Bankruptcy Code).

110. *Id.* at 6.

111. *Id.*

112. *Id.* (stating that while the debtors do retain a right to keep certain assets, usually much of what they own must be sold by an appointed trustee to pay the debtors’ liabilities).

113. *Id.* at 7–8. Entities that have filed for Chapter 9 protection include villages, counties, municipal utilities, and school districts. *Id.*

114. *Id.* at 7.

115. *Id.* The creditors must approve the debtor’s plan, which usually requires that the debtor’s business go through a period of consolidation before returning to profitability. *Id.*

116. *Id.*

propose a plan to pay off debts, but this Chapter is reserved to individuals with regular income lower than what is required to file under Chapter 11.¹¹⁷ Lastly, Chapter 15 provides mechanisms for adjudicating cross-border insolvencies.¹¹⁸ Chapters 7 and 11 are the most relevant to the present discussion because business trusts rarely file under any of the other chapters.¹¹⁹

2. The Code

The Bankruptcy Code goes to great lengths to define and limit the entities that have the benefit of bankruptcy protection.¹²⁰ Section 109 of the Code limits those who can file for Chapter 11 protections to “persons” who also qualify for chapter seven protections.¹²¹ The Code defines a “person” as including an “individual, partnership, and corporation, but does not include [a] governmental unit.”¹²² Additionally, § 109(d) restricts stockbrokers, commodity brokers, and railroads from filing for Chapter 11, while making specific provisions allowing corporations to file.¹²³ The business trust is specifically included in the definition of a corporation in the Bankruptcy Code.¹²⁴ However, while the Code provides many specific definitions, it does not define exactly what a business trust is or supply any criteria used to

117. *Id.* Individual debtors usually prefer to file under Chapter 13 versus Chapter 7 because Chapter 13 allows them a greater opportunity to hold on to valuable assets. *Id.* If the debtor cannot pay his or her debts under the proposed plan, the court will generally require the debtor to convert their case to Chapter 7. *Id.*

118. *Id.* at 8.

119. *See infra* Part III.B.2.

120. *See infra* notes 121–25.

121. *See* 11 U.S.C. § 109(b) (2012) (limiting the persons that can file for Chapter 11 to anyone who is not a railroad, insurance company, or bank). In addition, § 109(a) imposes a territorial requirement: “Notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title.” *Id.* § 109(a).

122. *Id.* § 101.

123. Text of § 109(d) reads:

Only a railroad, a person that may be a debtor under chapter 7 of this title [11 U.S.C. § 701] (except a stockbroker or a commodity broker), and an uninsured State member bank, or a corporation organized under section 25A of the Federal Reserve Act . . . which operates, or operates as, a multilateral clearing organization pursuant to section 409 of the Federal Deposit Insurance Corporation Improvement Act of 1991 may be a debtor under chapter 11 of this title.

Id. § 109(d).

124. *Id.* § 101.

determine when a trust is a business trust.¹²⁵

The history of the Bankruptcy Code may be able to shed some light on the absence of a definition for the business trust.¹²⁶ The original Bankruptcy Act enacted in 1898 did not mention business trusts.¹²⁷ However, in 1926, Congress amended the Act to include corporations and included within the definition of a corporation “any business conducted by a trustee or trustees wherein beneficial interest or ownership is evidenced by certificate or other written instrument.”¹²⁸ It was not until 1978 that the Bankruptcy Code made a specific provision for the inclusion of business trusts.¹²⁹ This new provision removed the requirement of a written certificate, and courts reasoned that Congress included business trusts in the Code because of their similarity to corporations.¹³⁰ In addition, because the definition of the business trust is included under the definition of a corporation, it is likely that Congress intended to include trusts that conducted business and did not merely hold property.¹³¹ Thus, the addition of the business trust to the Bankruptcy Code is relatively new.¹³² Due to the lack of any definition of a business trust in the Bankruptcy Code, courts have been forced to make determinations without the guidance of the legislature.¹³³ However, the leeway given to the courts has not

125. *Id.* The Code mentions the business trust under the definition of a corporation but does not define the business trust itself:

The term “corporation”—

(A) includes—

- (i) association having a power or privilege that a private corporation, but not an individual or a partnership, possesses;
- (ii) partnership association organized under a law that makes only the capital subscribed responsible for the debts of such association;
- (iii) joint-stock company;
- (iv) unincorporated company or association; or
- (v) business trust;

Id.

126. *See infra* notes 127–33.

127. *See* 1 WILLIAM L. NORTON JR., NORTON BANKRUPTCY LAW AND PRACTICE § 1:8, Westlaw (database updated Jan. 2016).

128. Bankruptcy Act of 1898, Pub. L. No. 62-57, § 1(8), 30 Stat. 544, 544 (1926).

129. David S. Jennis & Kathleen L. DiSanto, *Trust or Debtor: You Decide*, AM. BANKR. INST. J., Dec. 2013, at 34, 34.

130. *In re* Old Second Nat’l Bank of Aurora, 7 B.R. 37, 38 (Bankr. N.D. Ill. 1980).

131. *See In re* N. Shore Nat’l Bank of Chi., Land Tr. No. 362, 17 B.R. 867, 869–70 (Bankr. N.D. Ill. 1982).

132. *See* Jennis & DiSanto, *supra* note 129, at 34.

133. *See infra* Part III.B.3.

resulted in a clear definition of the business trust.¹³⁴

3. The Courts

When trying to tackle the issue of when a trust is a business trust, courts have come up with several different definitions of a business trust.¹³⁵ However, there are certain types of trusts that courts generally exclude from consideration as business trusts because of their inherent characteristics.¹³⁶ When confronted with these types of trusts, the courts employ a categorical approximation approach to remove the trust from consideration.¹³⁷ On the other hand, not all courts apply this approach but choose to perform a full analysis of the trust regardless of the label assigned to it.¹³⁸ This approach is hereinafter referred to as the general inquiry approach.¹³⁹

The categorical approximation approach labels the categories of trusts and categorically eliminates some of them from consideration as a business trust.¹⁴⁰ First, family trusts are excluded from consideration as a business trust under the categorical approximation approach because the general goal of the trust is to preserve the trust property.¹⁴¹ Courts have excluded family trusts from the

134. *See infra* Part III.B.3.

135. “The decisions are sharply, and perhaps hopelessly, divided on the meaning of ‘business trust.’” *In re Medallion Realty Tr.*, 103 B.R. 8, 10–11 (Bankr. D. Mass. 1989), *aff’d*, 120 B.R. 245 (D. Mass. 1990); *see, e.g., In re Arehart*, 52 B.R. 308 (Bankr. M.D. Fla. 1985) (finding a land trust with some business activities eligible); *In re Gonic Realty Tr.*, 50 B.R. 710 (Bankr. D.N.H. 1985) (finding a trust created for benefit of trustee and his wife, which owned and leased a mill complex, eligible); *In re Dolton Lodge Tr. No. 35188*, 22 B.R. 918 (Bankr. N.D. Ill. 1982) (finding a land trust with no business activities ineligible); *In re Dreske Greenway Tr.*, 14 B.R. 618 (Bankr. E.D. Wis. 1981) (finding a trust created to conduct business which in fact did so eligible); *In re Cohen*, 4 B.R. 201 (Bankr. S.D. Fla. 1980) (finding a land trust ineligible where it conducted minimal zoning and filling activities); *In re Treasure Island Land Tr.*, 2 B.R. 332 (M.D. Fla. 1980) (finding a land trust ineligible where declaration of trust prohibited business activities and trust was then engaging in none).

136. Takemi Ueno, Comment, *Defining a “Business Trust”: Proposed Amendment of Section 101(9) of the Bankruptcy Code*, 30 HARV. J. ON LEGIS. 499, 503–06 (1993) (describing the categorical approximation approach that attempts to first pose the question of which type of trust is at issue, then categorically eliminate certain types of trusts from consideration as business trusts).

137. *Id.*; *see also infra* notes 141–42.

138. *See Morrissey v. Comm’r*, 296 U.S. 344, 350–51 (1935) (favoring a more comprehensive approach with less emphasis in the type of trust and more focus on whether the trust is conducting business).

139. *See Loux v. Gabelhart (In re Carriage House, Inc.)*, 120 B.R. 754, 761–66 (Bankr. D. Vt. 1990) (foregoing the initial hurdle of the type of trust and instead conducting a full analysis); *see also* Ueno, *supra* note 136.

140. Ueno, *supra* note 136, at 503.

141. *Id.* Ueno defines a family trust as “both a traditional trust in which the corpus is preserved for

definition of a business trust even when the trust has a business purpose.¹⁴² Furthermore, courts also exclude land trusts from business trusts under the categorical approximation approach.¹⁴³ Under the typical land trust structure, the recorded deed gives the trustee the power to deal with the property.¹⁴⁴ Courts exclude this category because, like the family trust, the purpose of the land trust is to preserve the property for the benefit of the beneficiary.¹⁴⁵ Commentators have stated that if land trusts were eligible for bankruptcy as a business trust, it would lead to a fragmentation of the bankruptcy proceedings because “[a]n individual might, for example, file a reorganization case for ‘land trust’ property and a liquidation case for other property, resulting in differing treatment of creditors.”¹⁴⁶ Thus, under the categorical approximation approach, courts undertake no further inquiry into the business activities of the trust once the court establishes that the trust falls into one of the excluded categories.¹⁴⁷

In effect, the categorical approximation approach excludes some trusts that would be permitted to file for bankruptcy under the general inquiry approach because it looks only at the label of the trust and not the activities of the trust.¹⁴⁸ For instance, when applying the general inquiry approach, which consists of a totality of the circumstances analysis, the court found the family trust in *Loux v. Gabelhart* to be a business trust.¹⁴⁹ Under the categorical approximation

the comfort and maintenance of the beneficiaries—who are usually the settlor’s or grantor’s relatives—and a trust in which the trustees and beneficiaries are relatives or close friends.” *Id.* at 503 n.25.

142. See *In re Woodsville Realty Tr.*, 120 B.R. 2 (Bankr. D.N.H. 1990); *In re Margaret E. DeHoff Tr. I*, 114 B.R. 189 (Bankr. W.D. Mo. 1990); *In re Ralph Faber Tr.*, 113 B.R. 599 (Bankr. D.N.D. 1990); *In re Ophir Tr.*, 112 B.R. 956 (Bankr. E.D. Wis. 1990); *In re St. Augustine Tr.*, 109 B.R. 494 (Bankr. M.D. Fla. 1990); *In re Vivian A. Skaife Irrevocable Tr. No. 1*, 90 B.R. 325 (Bankr. E.D. Tenn. 1988); *In re Johnson*, 82 B.R. 618 (Bankr. S.D. Fla. 1988); *In re Walker*, 79 B.R. 59 (Bankr. M.D. Fla. 1987); *In re Milani Family Irrevocable Tr.*, 62 B.R. 6 (Bankr. S.D. Fla. 1986); *In re L & V Realty Tr.*, 61 B.R. 423 (Bankr. D. Mass. 1986); *In re Jay M. Weisman Irrevocable Children’s Tr. of 1981*, 62 B.R. 286 (Bankr. M.D. Fla. 1981).

143. Ueno, *supra* note 136, at 504; see also *In re Dolton Lodge Tr. No. 35188*, 22 B.R. 918 (Bankr. N.D. Ill. 1982); *In re N. Shore Nat’l Bank of Chi., Land Tr. No. 362*, 17 B.R. 867 (Bankr. N.D. Ill. 1982); *In re Citizens Bank & Tr. Co.*, 8 B.R. 812 (N.D. Ill. 1981); *In re Old Second Nat’l Bank*, 7 B.R. 37 (Bankr. N.D. Ill. 1980); *In re Cohen*, 4 B.R. 201 (Bankr. S.D. Fla. 1980); *In re Treasure Island Land Tr.*, 2 B.R. 332 (Bankr. M.D. Fla. 1980).

144. *Trust*, BLACK’S LAW DICTIONARY, *supra* note 98.

145. Ueno, *supra* note 136, at 504.

146. *Id.* (citing WILLIAM NORTON, JR., NORTON BANKRUPTCY LAW AND PRACTICE § 8.08 (1992) (attempting to provide credence to the categorical approximation approach and an example for why land trust should be ineligible for bankruptcy protection)).

147. See *id.* at 503–06.

148. See *supra* notes 141–47 and accompanying text.

149. *Loux v. Gabelhart (In re Carriage House, Inc.)*, 120 B.R. 754, 766 (Bankr. D. Vt. 1990).

approach, the court would consider this trust excluded and the analysis would end there.¹⁵⁰ In *Loux*, creditors sought to include the family trust property in the debtors' personal bankruptcy estate.¹⁵¹ The court, applying a general inquiry approach, reasoned that the trust is a business trust because the trust-executing instrument simply labeled the trust as a real estate investment trust.¹⁵² Therefore, the trust had to file separately for bankruptcy and the trust property was out of the reach of the debtors' personal creditors.¹⁵³

In addition, courts have found land trusts to be business trusts in certain instances when applying the general inquiry approach.¹⁵⁴ In *In re Arehart*, the court found that a business trust was formed where a land trust instrument stated that the purpose of the trust was "to acquire, develop, improve, operate, lease, and/or sell the trust lands . . . to the economic benefit of the beneficiaries."¹⁵⁵ The court did not dismiss the trust merely because it was a land trust but analyzed the current operations of the trust in its determination.¹⁵⁶

These cases show that the categorical approximation approach takes a narrower viewpoint than the general inquiry approach, which has the effect of limiting the amount of trusts that meet the business trust criteria.¹⁵⁷ Most courts favor the general inquiry approach over the categorical approximation approach because it allows courts to consider the totality of the circumstances without having to rely on the preliminary question of what type of trust is at issue.¹⁵⁸ Moreover, the categorical approximation approach may be obsolete because its reasoning is that the trusts that are excluded generally do not conduct business, the same conclusion that a court applying a general inquiry approach would have come to.¹⁵⁹ For instance, courts exclude family trusts and land trusts under the categorical approximation approach because those trusts generally do not conduct business but rather hold property for beneficiaries.¹⁶⁰ However,

150. See *supra* note 142 and accompanying text.

151. *Loux*, 120 B.R. at 756.

152. *Id.* at 758.

153. *Id.*

154. See *infra* notes 155–56 and accompanying text.

155. 52 B.R. 308, 308 (Bankr. M.D. Fla. 1985).

156. *Id.*

157. See also Ueno, *supra* note 136, at 506 (describing the framework of the categorical approximation approach). Compare *In re Arehart*, with *Loux*, 120 B.R. at 754.

158. See *Morrissey v. Comm'r*, 296 U.S. 344, 350–51 (1935) (favoring a more comprehensive approach with less emphasis in the type of trust and more focus on whether the trust is conducting business).

159. Ueno, *supra* note 136.

160. See *supra* notes 141–43 and accompanying text.

“[c]ourts rarely conclude that a trust is eligible to be a debtor simply because of its category; rather, they find that a trust is a business trust on a case-by-case basis.”¹⁶¹ Thus, even though the categorical approximation approach exists, courts tend to employ a general inquiry approach because the categorical approximation approach excludes some trusts that conduct business.¹⁶²

The general inquiry approach is the umbrella term for the various approaches courts use that, although different in some respects, apply totality of the circumstances inquiries.¹⁶³ While most courts agree that a business trust must conduct business, this is where the similarities between the approaches end.¹⁶⁴

Some bankruptcy courts apply the test enunciated in *Morrissey*, which applied the federal income tax definition of a corporation.¹⁶⁵ In *Morrissey*, the trustees of an insolvent golf course failed to pay income taxes for the years 1924–1926.¹⁶⁶ The trustees contended that the IRS had been illegally treating the trust as an association and therefore no taxes were due.¹⁶⁷ In holding that the trust was subject to tax, the court found the trust to be a corporation for tax purposes because it had: (1) business functions, (2) transferable certificates of beneficial interest, (3) centralized management, (4) continuity of life, and (5) limited liability.¹⁶⁸ In sum, the court found that the trust was created for the purpose of developing a tract of land and issued transferable shares sufficient to meet the federal income tax definition.¹⁶⁹

Earlier, the Supreme Court applied a similar tax-based approach in *Hecht*.¹⁷⁰ In *Hecht*, there were four trusts at issue and the Court was required to

161. Ueno, *supra* note 136, at 506.

162. See *supra* note 136 and accompanying text.

163. See *In re Star Tr.*, 237 B.R. 827, 831 (Bankr. M.D. Fla. 1999) (concluding that in deciding whether a trust qualifies as a business trust, the focus should be on the totality of the circumstances).

164. See *Shawmut Bank Conn., Nat'l Ass'n LNC Invs., Inc. v. First Fid. Bank (In re Secured Equip. Tr. of E. Air Lines, Inc.)*, 38 F.3d 86, 89 (2d Cir. 1994) (“Ultimately, each decision is based on a very fact-specific analysis of the trust at issue.”); *Cutler v. The 65 Sec. Plan*, 831 F. Supp. 1008, 1014 (E.D.N.Y. 1993) (“The decisions [regarding business trusts] are, in fact, ‘hopelessly divided.’”).

165. *Morrissey v. Comm’r*, 296 U.S. 344 (1935); see also *Mosby v. Boatmen’s Bank of St. Louis Cty. (In re Mosby)*, 61 B.R. 636, 638 (E.D. Mo. 1985) (applying the same test based on federal income tax law).

166. *Morrissey*, 296 U.S. at 346.

167. *Id.*

168. *Id.* at 359; see also *Mosby*, 61 B.R. at 638 (applying the same test).

169. See *Morrissey*, 296 U.S. at 360.

170. *Hecht v. Malley*, 265 U.S. 144 (1925). Here, the Court was applying a tax-based approach because it was faced with a federal income tax issue. *Id.* at 145. Bankruptcy courts have adopted this approach because it provides a quick fix to the uncertainty as to which test should govern their

determine whether a corporate tax could be excised on the trusts.¹⁷¹ Although the trusts were not registered under state law as corporations, they did fall under the category of a Massachusetts business trust under federal income tax law.¹⁷² However, the Court only held that the trusts at issue were subject to tax because they performed business activities and thus were an association under the tax code.¹⁷³ The Court did not determine the criteria for determining when a trust is a business trust in other contexts.¹⁷⁴

More recently, bankruptcy courts have asked whether the trusts are currently performing business-like activities to determine whether they are a business trust.¹⁷⁵ These cases place a large emphasis on current activity, asking whether that activity is for profit or merely to preserve the trust property.¹⁷⁶ For instance, in *In re Arehart*, the court held that the trust was conducting business-like activities sufficient to be considered a business trust.¹⁷⁷ The court noted that the purpose of the trust in the executing instrument was not to preserve the trust assets but rather to sell the trust property.¹⁷⁸ Additionally, the trustee had substantial management powers and was subject to little control of the beneficiaries and shareholders.¹⁷⁹ In *In re Arehart*, the court reached its conclusion without applying any pre-set test but rather by applying the nebulous approach of analyzing the factual circumstances before it.¹⁸⁰

In a more recent case, *In re Star Trust*, the court concluded that the focus of the business trust inquiry is whether the trust documents, not the current

determination. See *Mosby*, 61 B.R. at 636.

171. *Hecht*, 265 U.S. at 145.

172. *Id.* at 157.

173. *Id.* at 161–62.

174. *Id.*

175. See, e.g., *In re Gonic Realty Tr.*, 50 B.R. 710, 714 (Bankr. D.N.H. 1985) (finding a trust created for benefit of the trustee and his wife, who owned and leased a mill complex eligible); *In re Dolton Lodge Tr. No. 35188*, 22 B.R. 918, 926 (Bankr. N.D. Ill. 1982) (finding a land trust with no business activities ineligible); *In re Dreske Greenway Tr.*, 14 B.R. 618, 623 (Bankr. E.D. Wis. 1981) (finding a trust created to conduct business, which in fact did so, eligible).

176. See *supra* note 175 and accompanying text.

177. 52 B.R. 308, 311 (Bankr. M.D. Fla. 1985).

178. *Id.* at 310.

179. *Id.* This finding is similar to the holding in *Williams* where the court described the trustees as the “masters” of the trust property. *Williams v. Inhabitants of Milton*, 102 N.E. 355, 357 (Mass. 1913). This is significant because the degree of control exhibited by the trustee is a major characteristic of the business trust. See *infra* Part IV.B (attempting to incorporate the history of the business trust into a proposed test).

180. *In re Arehart*, 52 B.R. at 308.

operations, indicate whether the trust is a business trust.¹⁸¹ In *In re Star Trust*, there were two trusts that held real estate for development.¹⁸² The court, in addition to looking to *Morrissey* for guidance, placed great importance on the trust agreement.¹⁸³ However, the trust terms cited did not state that the trust was created for business purposes; rather, the court reasoned that the trust was a business trust because the agreement did not list preservation of trust assets as a purpose.¹⁸⁴ The *In re Star Trust* decision is important because throughout the court's discussion of the business trust, it was trying to pull together all possible materials in order to reach its conclusion.¹⁸⁵ Ultimately, the court attempted to combine approaches from several previous cases and supplement them with its own approach to draw a conclusion.¹⁸⁶ However, the *In re Arehart* and *In re Star Trust* courts' approaches are not conducive to creating a consistent precedent for future courts to apply because they placed varying degrees of emphasis on separate factors in making their determinations.¹⁸⁷

In a different approach, the court in *In re Cohen* formulated a twenty-four-point test to determine whether a trust was a business trust.¹⁸⁸ In *In re Cohen*,

181. 237 B.R. 827, 832 (Bankr. M.D. Fla. 1999).

182. *Id.*

183. *Id.*

184. *Id.* The trust agreement cited by the court is as follows: "PURPOSE AND INTENT. The purpose and intent of this trust is to avoid probate, facilitate the cost and ease of transfer of the property, keep property assessments down and help in the estate planning of the Grantor and/or Beneficiary." *Id.* The court reasoned further that because the trust distributed property at death, it was a continuous instrument and similar to a corporation in that regard and, therefore, a business trust. *Id.*

185. *Id.* at 831–32 (attempting to combine tests analyzing the current operations of the trust, the trust instrument and federal income tax law).

186. *Id.*

187. Compare *In re Star Tr.*, 237 B.R. 827, with *In re Arehart*, 52 B.R. 308 (Bankr. M.D. Fla. 1985). See generally Ueno, *supra* note 136.

188. 4 B.R. 201, 203–04 (Bankr. S.D. Fla. 1980). The court does not specifically list the items as factors but as findings of fact; however, other courts have specifically relied on them as factors in making their decisions. See *In re Arehart*, 52 B.R. at 308 (using the findings listed in *In re Cohen* to formulate a factor test off of which it based its analysis). The points emphasized by the *In re Cohen* court are: (1) whether the trust filed for an occupational license as a business; (2) whether the trustee was acting under a fictitious name; (3) whether the trust filed separate tax returns and paid corporate income taxes; (4) whether the trust had income; (5) whether the trust instrument indicated an ongoing business; (6) whether the trust instrument was executed before operation commenced (if so, it indicated that the trust does not have an independent business purpose); (7) whether the trustee had control of the disbursements or if the trust disbursed all property to the beneficiaries; (8) whether there were any previous disbursements to the beneficiaries; (9) whether the operation headquarters of the trust looked like a business; (10) whether the trust was separate physically and had separate physical assets; (11) whether the trust issued financial or operating statements to beneficiaries; (12) whether the trust had loans or extensions of credit other than a mortgage on the trust property; (13) whether the trust

the trust controlled a single vacant and undeveloped lot.¹⁸⁹ The only activity in relation to the trust property was filling and bulk-heading efforts by non-trustees.¹⁹⁰ However, the court formulated a twenty-four-point test to determine whether the trust was a business trust.¹⁹¹ The court went as far as to ask whether the trust had separate stationary.¹⁹² With such diverse precedent and no uniform test, courts have no other choice but to formulate their own approach, which potentially explains why there is such a diverse array of approaches in this particular area of the law.¹⁹³

IV. THE PROPOSITION

A. Uniformity of Law

The vast differentiation among the courts' analyses leads to confusion and unnecessary litigation.¹⁹⁴ A uniform approach adopted by the courts is the best solution to this problem.¹⁹⁵ In order to cure the issue under a different approach, commentators have proposed that the definition of a business trust in bankruptcy be intimately linked with the definition of the business trust in the relevant state.¹⁹⁶ Courts have also supported this proposition.¹⁹⁷ In *In re*

developed the trust property; (14) whether the trust had an independent bank account; (15) whether there were any formal meetings of the beneficiaries; (16) whether the trust was a close family enterprise; (17) whether the beneficiaries' interests were freely transferable; (18) whether the trust collected rent from real property in its possession; (19) whether the trust borrowed money; (20) whether the trust wrote a check; (21) whether the trust had a budget; (22) whether the trust had independent accounting records; (23) whether the trust had an independent name for operating purposes; and (24) whether the trust instrument indicated that the property is to be held in trust. *In re Cohen*, 4 B.R. at 203–04.

189. *In re Cohen*, 4 B.R. at 202.

190. *Id.* “A bulkhead is a retaining wall, such as a bulkhead within a ship or a watershed retaining wall. It may also be used in mines, to contain flooding.” *Bulkhead*, WIKIPEDIA, [http://en.wikipedia.org/wiki/Bulkhead_\(barrier\)](http://en.wikipedia.org/wiki/Bulkhead_(barrier)) (last modified Jan. 31, 2014, 11:01 PM).

191. *In re Cohen*, 4 B.R. at 203–04.

192. *Id.* at 203.

193. *See Cutler v. The 65 Sec. Plan*, 831 F. Supp. 1008, 1014 (E.D.N.Y. 1993) (“A uniform body of law has not resulted . . . [and] [t]he decisions are, in fact, ‘hopelessly divided.’”).

194. *See generally* Ueno, *supra* note 136.

195. *See infra* note 200.

196. Ueno, *supra* note 136, at 514 (proposing that the definition of a business trust be determined by the applicable definition in the state in which the trust is located). Ueno states that current case law as well as state statutes may not address this issue. *Id.* However, the cost of accounting for these states would not outweigh the benefit of increased efficiency for the bankruptcy courts. *Id.* Ueno reasons that if the law were based on current state statutes, it would be clear enough to prevent non-business trusts to file in hopes that they would be granted protection. *Id.* at 515. Ueno also offers Securities and

Village Green Realty Trust, the court recognized that the Code did not offer a definition of a business trust and turned to the relevant state law for guidance.¹⁹⁸ However, this solution does not comport with the United States Constitution or the intentions of the Framers.¹⁹⁹

Article I, Section 8 of the United States Constitution grants Congress the power to create “uniform Laws on the subject of Bankruptcies throughout the United States.”²⁰⁰ When writing this particular Section of the Constitution, the Framers were concerned with the current “patchwork of different bankruptcy laws among the states, including the fact that debtors who had been discharged from debts in one state could be imprisoned for the same debts upon travelling to another state.”²⁰¹ Thus, Congress should not allow a piece of the federal Bankruptcy Code to rely so heavily on state law because it would again result in a patchwork of state laws that the Framers intended to remedy when they wrote the Constitution.²⁰² Additionally, the resulting patchwork would lead to further confusion as to which state’s law would apply to trusts that have dealings in multiple states.²⁰³ Furthermore, the very definition of the term “uniform” includes consistent in conduct or opinion,²⁰⁴ and it is the inconsistency of the current system that is causing confusion and inefficiency.²⁰⁵ Such reliance on state law would not solve the problem but would merely shift the source of the confusion from competing tests to competing state law.²⁰⁶

Exchange Commission (SEC) regulations as an alternative to state regulation; however, many trusts are not large enough to be covered by the SEC (they are not publicly traded) and the problem would remain largely unsolved. *Id.* at 514. Additionally, Ueno does not discuss the potential issues related to trusts that have dealings in multiple states and which state’s laws would be applied.

197. *See infra* note 201 and accompanying text.

198. 113 B.R. 105, 113 (Bankr. D. Mass. 1990) (“[S]ince the decisions are, if not hopelessly divided, at least certainly divergent, this Court must look, to state law for guidance.”); *see also In re Heritage N. Dunlap Tr.*, 120 B.R. 252, 254 (Bankr. D. Mass. 1990) (“Since the Code does not define what constitutes a business trust, we look to state law.”).

199. *See infra* notes 200–06 and accompanying text.

200. U.S. CONST. art I, § 8, cl. 4. The entire clause reads: “To establish a uniform Rule on Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States.” *Id.*

201. Daniel A. Austin, *Bankruptcy and the Myth of “Uniform Laws”*, 42 SETON HALL L. REV. 1081, 1152 (2012).

202. *See id.*

203. *See supra* note 196 and accompanying text.

204. *Uniform*, MERRIAM-WEBSTER, <http://merriam-webster.com/dictionary/uniform> (last visited Mar. 10, 2016).

205. *See supra* Part III.B.3.

206. *See supra* Part III.B.3 (discussing the various tests employed by the courts and the confusion they have created, relying on fifty separate state laws would not remedy this confusion); *see also supra*

Case law also supports the conclusion that relying on state law for the definition of a business trust would not reduce confusion.²⁰⁷ In *Brady-Morris v. Schilling*, the court tackled the issue of whether the state law definition of a business trust should apply.²⁰⁸ The court reasoned that federal law would provide a better and more consistent outcome than state law because the application of state law could have potentially differing results.²⁰⁹ With all the confusion associated with precedent, it is safe to assume that the court believed reliance on state law would result in even greater confusion.²¹⁰ However, the court in *In re Arehart* explained the issues with the application of state law best:

Whether an entity is eligible for relief under Title 11 of the United States Code is purely a matter of federal law. To hold otherwise would result in different results in different states and an entity would be eligible for relief in one state but not in another. Clearly this is not what Congress intended when it enacted the bankruptcy laws in this country in conformity with the mandate of Article I, Section eight of the Constitution, which provides that “Congress shall have the power . . . to establish . . . uniform laws on the subject of bankruptcies.”²¹¹

Thus, relying on state law would not only cause more confusion but would also contradict the intention of the Framers and the text of the Constitution.²¹² In order to ensure a consistent application of the uniform law of bankruptcies, courts should adopt and apply a single test.²¹³

note 196 and accompanying text.

207. See *infra* notes 208–11 and accompanying text (describing the folly of relying on state law); see also *In re Sung Soo Rim Irrevocable Intervivos Tr.*, 177 B.R. 673, 676 (Bankr. C.D. Cal. 1995) (“[T]he availability of access to the federal bankruptcy courts and the availability of bankruptcy relief itself are ultimately questions of federal, not state, law.”); *In re Woodsville Realty Tr.*, 120 B.R. 2, 4 n.2 (Bankr. D.N.H. 1990) (“[I]n the absence of [any] explicit contrary Congressional intent, the Bankruptcy Code definition of qualified trust debtors was to be developed on a uniform national basis by case-by-case adjudication.”).

208. *Brady-Morris v. Schilling* (*In re Kenneth Allen Knight Tr.*), 303 F.3d 671, 678 (6th Cir. 2002).

209. *Id.* at 676–77.

210. See *supra* Part III (outlining the conflicting approaches of the courts); see also *supra* note 207 and accompanying text.

211. *In re Arehart*, 52 B.R. 308, 310–11 (Bankr. M.D. Fla. 1985); see also U.S. CONST. art. I, § 8, cl. 4.

212. See *supra* notes 201–11 and accompanying text.

213. See *infra* Part IV.B.

B. Proposed Four-Factor Restatement Test

The test proposed here not only attempts to set forth a generally applicable test for the determination of bankruptcy trusts, but also serves as a restatement of the law.²¹⁴ Each proposed factor bears in mind the history of the business trust, as well as the prior applications by various courts that have tackled this issue.²¹⁵ In order to settle on a consistent test for the courts to apply, it is important to be cognizant of the history of the business trust and its practical uses.²¹⁶ For instance, the restatement test does not simply define a business trust as a corporation in trust form because the history of the business trust indicates that one of its uses is to circumvent strict incorporation statutes.²¹⁷ Additionally, the practical characteristics of the business trust were taken into account in proposing this comprehensive restatement test so as not to alter the form and benefits of the business trust.²¹⁸ Thus, the proposed restatement test allows the trustee to remain the “master” of the trust.²¹⁹ Furthermore, the proposed restatement test should not destroy the trustee’s benefit of limited liability, which is common to the trust structure.²²⁰

After these considerations are taken into account along with courts’ previous approaches, the proposed restatement test regarding business trusts should be a factor-based test with the following factors: (1) a voluntary pooling of capital with freely transferable shares; (2) presence of creditors; (3) profit-making purpose; and (4) current business operations.²²¹ Nearly all courts that have tackled this issue agree that the primary purpose of a business trust

214. See *infra* Part IV.B.1–4 (listing and justifying the four factors that comprise the test proposed by this Comment).

215. See *infra* Part IV.B.1–4.

216. See *supra* Part II.

217. See *supra* Part II.

218. See *infra* Part IV.B.1–4.

219. See *Williams v. Inhabitants of Milton*, 102 N.E. 355, 357 (Mass. 1913) (describing the trustee–beneficiary relationship as the trustees being “masters” of the trust property).

220. See *supra* Part II; see also *Larson v. Sylvester*, 185 N.E. 44 (Mass. 1933).

221. The proposed factors most closely resemble the factors in *In re Joobeen*, 385 B.R. 599 (Bankr. E.D. Pa. 2008). The test in *In re Joobeen* is as follows:

- (1) the trust was formed for the primary purpose of transacting business or commercial activity, as opposed to preserving assets;
- (2) the trust was formed by a group of investors who contribute capital to the enterprise with the expectation of receiving a return on their investment;
- (3) the trust was created in compliance with state law; and
- (4) the beneficial interests of the trust must be freely transferable.

Id. at 613 (citing *In re Eagle Tr.*, No. 97-23298, 1998 WL 635845, at *5 (E.D. Pa. Sept. 16, 1998)). However, the factor test proposed here places no reliance on state law and presents nuances that are not a characteristic of the *In re Joobeen* test. See *infra* Part IV.B.1–4.

remains the performance of business; these factors create a consistent vehicle for the courts to evaluate the characteristics of the trust to determine if the trust is, in fact, conducting sufficient business.²²²

1. Voluntary Pooling of Capital with Freely Transferable Shares

This factor asks whether the beneficiaries of the trust have contributed something of value to the trust.²²³ The trust must issue transferable shares in exchange for an equity stake in the trust.²²⁴ In this instance, the beneficiaries who have purchased shares in the trust are very similar to stockholders of a corporation who own equity in the company.²²⁵ However, unlike a corporation, the trustee has more power over the dealings of the trust.²²⁶ Therefore, unlike the officers of a corporation who are often subject to the scrutiny of the shareholders, the trustee is the “master” of the trust.²²⁷

The benefits that the trustee of a business trust enjoys include, but are not limited to: the ability of the trustee to affect a reverse split of stocks or consolidation of stocks, greater control over stockholder meetings, and the ability to sell assets of the trust or amend the declaration of trust without the approval of the beneficiaries.²²⁸ Similar functions of a corporation are subject

222. See *infra* Part IV.B.1–4.

223. See *supra* note 221 and accompanying text (describing the necessity for transferable shares as previously recognized by the courts but also incorporating the history of the business trust into its current treatment).

224. “The business trust is a voluntary pooling of capital by a number of people who are the holders of freely transferable certificates evidencing beneficial interests in the trust estate. The holders are entitled to the same limitation of personal liability extended to stockholders of private corporations.” *In re Walker*, 79 B.R. 59, 61–62 (Bankr. M.D. Fla. 1987). Several other cases have stated that in order for trusts to be considered a business trust, it must issue transferable shares. See, e.g., *In re Medallion Realty Tr.*, 103 B.R. 8, 11 (Bankr. D. Mass. 1989) (“Congress intended to permit bankruptcy relief for all trusts which are created for the purpose of transacting business and whose beneficiaries make a contribution in money or money’s worth to the enterprise.”), *aff’d*, 120 B.R. 245 (D. Mass. 1990); *Mosby v. Boatmen’s Bank of St. Louis Cty.* (*In re Mosby*), 46 B.R. 175 (Bankr. E.D. Mo. 1985); *In re Treasure Island Land Tr.*, 2 B.R. 332 (Bankr. M.D. Fla. 1980).

225. ALAN R. PALMITER & FRANK PARTNOY, CORPORATIONS: A CONTEMPORARY APPROACH 33 (2d ed. 2010) (“[S]hareholders contribute capital to the corporation in exchange for ‘common shares’ of the corporation. These common shares represents a divided ownership stake in the corporation. Common shares typically entitle shareholders to certain financial claims on the corporation’s income.”).

226. See *infra* note 227 and accompanying text.

227. See *Williams v. Inhabitants of Milton*, 102 N.E. 355, 357 (Mass. 1913). “In nearly all cases, trusts which have been denied status as business trusts under the Bankruptcy Code have been ‘simple land trusts’ created under trust agreements that *strictly limited the authority of the trustees.*” *Merrill v. Allen* (*In re Universal Clearing House Co.*), 60 B.R. 985, 992 (Bankr. D. Utah 1986) (emphasis added).

228. *Jones*, *supra* note 29, at 458.

to a shareholder vote and approval.²²⁹ Therefore, this factor keeps in mind that a business trust, while similar to a corporation, is not the same and allows the trustee benefits that a corporate structure does not.²³⁰ This distinction is important because the creation of the business trust was motivated by its ability to circumvent strict incorporation statutes.²³¹ Thus, one of the main beneficial characteristics of the business trust is that it is not a corporation.²³²

Additionally, the shares in the trust must be freely transferable.²³³ In a publicly traded corporation, this takes place on the stock exchange and similar stock trading markets; however, in a business trust, it must simply take place freely.²³⁴ When the court applies this factor, it must be wary of hurdles that the beneficiaries must overcome in order to sell the shares in the trust. If the shares are not freely transferable, the trustee could show that the primary purpose of the trust is not profit but rather maintaining its current beneficiaries.²³⁵ If this were the case, the trust would most likely meet the criteria of a family or land trust and fail to meet the requirements of a business trust because the purpose of the trust would be to preserve the trust property and beneficiaries.²³⁶

Several courts agree that a voluntary pooling of capital with freely transferable shares is essential to the categorization of a trust as a business trust.²³⁷ In *In re Treasure Island Land Trust*, the court found that a land trust organized under Illinois law did not meet the criteria of a business trust.²³⁸ However, the court did not look to Illinois law for the definition of a trust but formulated its own test.²³⁹ The court noted that the trust had beneficial interests similar to stocks in a corporation in that they were “equal in value, held by a

229. See PALMITER & PARTNOY, *supra* note 225.

230. *Id.*

231. See *supra* Part II (describing the motivations for the genesis of the business trust in England and Massachusetts).

232. See PALMITER & PARTNOY, *supra* note 225.

233. See, e.g., *In re Medallion Realty Tr.*, 103 B.R. 8 (Bankr. D. Mass. 1989), *aff'd*, 120 B.R. 245 (D. Mass. 1990); *Mosby v. Boatmen's Bank of St. Louis Cty.* (*In re Mosby*), 46 B.R. 175 (Bankr. E.D. Mo. 1985); *In re Treasure Island Land Tr.*, 2 B.R. 332 (Bankr. M.D. Fla. 1980).

234. See PALMITER & PARTNOY, *supra* note 225, at 31.

235. See *In re Mohan Kutty Tr.*, 134 B.R. 987, 989 (Bankr. M.D. Fla. 1991) (referencing the absence of transferable shares as a large factor in the court's decision not to grant bankruptcy protection to the trust).

236. See *supra* Part III.B.3.

237. See, e.g., *In re Medallion Realty Tr.*, 103 B.R. at 11; *Mosby*, 46 B.R. at 175; *In re Treasure Island Land Tr.*, 2 B.R. at 334.

238. *In re Treasure Island Land Tr.*, 2 B.R. at 336.

239. *Id.*

large number of people in varying amounts, and [were] transferable.”²⁴⁰ However, even though the court reasoned that the trust indeed possessed transferable shares, it was not a business trust because of the language in the trust instrument.²⁴¹ The trust instrument stated: “The objects and purposes of this Trust shall be to hold title to the trust property and to protect and conserve it until its sale or other disposition or liquidation.”²⁴² Thus, the presence of transferable shares was not sufficient to overcome the language in the trust instrument, which stated a purpose of preservation rather than business.²⁴³ The analysis in *In re Treasure Island Land Trust* is precisely the reason this Comment proposes a factor-based approach, where the court weighs each factor in comparison with the others, versus an element-based approach, where each prong is evaluated in isolation.²⁴⁴ Thus, the presence of transferable shares does not automatically make a trust a business trust; likewise, if a trust does not have transferable shares, it does not automatically prevent it from becoming a business trust. However, the absence of a factor will weigh heavily in favor of the court finding that the trust is not a business trust.²⁴⁵ Thus, each factor is weighed in accordance with the others to determine if the trust is conducting sufficient business to be considered a business trust.

Similarly, in *Mosby v. Boatmen’s Bank of St. Louis County*, the court found the presence of transferable shares as evidence that the trust was conducting business.²⁴⁶ In *Mosby*, the court reasoned that a business trust is “in the nature of a corporation” and thus should have transferable shares reflecting interests in the trust.²⁴⁷ In return for their investment, the shareholders “enjoy varying degrees of limited personal liability for the obligations which may arise from operation of the business trust.”²⁴⁸ Yet even though the trust possessed transferable shares, the trustee was not required to engage in any particular

240. *Id.* at 334.

241. *Id.*

242. *Id.*

243. *See id.*

244. *See infra* Part IV.C.

245. *See In re Mohan Kutty Tr.*, 134 B.R. 987, 989 (Bankr. M.D. Fla. 1991) (referencing the absence of transferable shares as a large factor in the court’s decision not to grant bankruptcy protection to the trust).

246. *Mosby v. Boatmen’s Bank of St. Louis Cty.* (*In re Mosby*), 46 B.R. 175, 178 (Bankr. E.D. Mo. 1985)

247. *Id.* at 177.

248. *Id.*; *see also* *Associated Cemetery Mgmt., Inc. v. Barnes*, 268 F.2d 97 (8th Cir. 1959) (evaluating the presence of transferable shares); *In re Armstead and Margaret Wayson Tr.*, 29 B.R. 58 (Bankr. D. Md. 1982); *In re John M. Cahill, M.D. Assocs. Pension Plan*, 15 B.R. 639 (Bankr. E.D. Pa. 1981).

business and was allowed to conduct the affairs by simply preserving the trust property.²⁴⁹ This is another example of when the presence of transferable shares on its own does not show that the trust is conducting sufficient business.²⁵⁰ Yet, the absence of transferable shares can be a considerable factor in determining that a trust is not a business trust.²⁵¹ In *In re Mohan Kutty*, the court reasoned that the trust was not conducting business, and a factor in its decision was that the trust did not issue transferable shares.²⁵²

Thus, the transferable shares factor is by no means dispositive but can indicate the presence of business activities necessary for a business trust.²⁵³ This factor is necessary to a complete restatement test because it protects the trustee's powers under the business trust structure and allows the business trust to remain similar to, yet distinct from, a corporation.²⁵⁴ This factor also partially incorporates the test proposed in *Morrissey*, which required transferable certificates of beneficial interest.²⁵⁵ Additionally, this factor upholds the intention of Congress, which sought to grant business trusts bankruptcy protections because of their similarity to corporations, and transferable shares are such a similarity.²⁵⁶

2. Presence of Creditors

The presence of creditors may seem obvious in the context of bankruptcy because in order to file for bankruptcy, the debtor must be insolvent to some

249. *Mosby*, 46 B.R. at 178.

250. *Compare id.*, with *In re Treasure Island Land Tr.*, 2 B.R. 332 (Bankr. M.D. Fla. 1980).

251. *See In re Mohan Kutty Tr.*, 134 B.R. 987, 989 (Bankr. M.D. Fla. 1991).

252. *Id.*; *see also In re L & V Realty Tr.*, 61 B.R. 423, 424 (Bankr. D. Mass. 1986) (finding the lack of transferable certificates as strong evidence that the trust was not a business trust).

253. *See, e.g., In re Medallion Realty Tr.*, 103 B.R. 8 (Bankr. D. Mass. 1989), *aff'd*, 120 B.R. 245 (D. Mass. 1990); *In re Walker*, 79 B.R. 59, 61–62 (Bankr. M.D. Fla. 1987) (“The business trust is a voluntary pooling of capital by a number of people who are the holders of freely transferable certificates evidencing beneficial interests in the trust estate. The holders are entitled to the same limitation of personal liability extended to stockholders of private corporations.”); *Mosby*, 46 B.R. 175; *In re Treasure Island Land Tr.*, 2 B.R. at 332.

254. *See supra* Part II.

255. *See generally Morrissey v. Comm’r*, 296 U.S. 344 (1935) (proposing a test based on the federal income tax definition of a corporation).

256. “Congress intended to permit bankruptcy relief for all trusts which are created for the purpose of transacting business and whose beneficiaries make a contribution in money or money’s worth to the enterprise.” *In re Medallion Realty Tr.*, 103 B.R. at 11; *see also In re N. Shore Nat’l Bank of Chi.*, Land Tr. No. 362, 17 B.R. 867 (Bankr. N.D. Ill. 1982); *In re John M. Cahill, M.D. Assocs. Pension Plan*, 15 B.R. 639 (Bankr. E.D. Pa. 1981).

extent.²⁵⁷ However, the presence of creditors, especially unsecured trade creditors, can serve as evidence that the trust was engaged in business and not merely holding property.²⁵⁸ Additionally, several courts have looked to the presence of creditors in their determination of whether the trust in question was a business trust.²⁵⁹

An unsecured debt is not secured by any collateral and is inherently riskier for lenders because there is no asset to recover in the event of a default.²⁶⁰ A secured debt is the opposite of an unsecured debt in that it is secured by an asset or collateral recoverable by the lender.²⁶¹ To take out an unsecured loan, the borrower must convince the lender that the borrower can repay the loan based on current financial resources.²⁶² The borrower often must show that he is, and has been, profitable in order to convince the lender to loan him the money.²⁶³ Such evidence of profitability generally points to an engagement in business.²⁶⁴ For example, in *In re Arehart*, the court found the presence of unsecured debt as evidence pointing in favor of the trust engaging in business.²⁶⁵ However, the presence of general unsecured debt does not always point to business dealings.²⁶⁶ In *In re Treasure Island Land Trust*, the court found that even though there were unsecured creditors, the lack of trade creditors showed that the trust was likely not engaged in business.²⁶⁷ Therefore, the best evidence of engagement in business under this prong is the presence of unsecured trade creditors because they are the best indication of

257. *See supra* Part III.B.1.

258. *See infra* note 265 and accompanying text.

259. *See, e.g., In re Star Tr.*, 237 B.R. 827, 837 (Bankr. M.D. Fla. 1999); *In re Arehart*, 52 B.R. 308 (Bankr. M.D. Fla. 1985); *In re Treasure Island Land Tr.*, 2 B.R. 332, 335 (Bankr. M.D. Fla. 1980).

260. *Secured v. Unsecured Loans*, GREENPATH DEBT SOLUTIONS, <http://www.greenpath.com/resources-tools/financial-library/loan-types/secured-vs-unsecured-loans> (last visited Mar. 10, 2016). Common examples of unsecured debt include credit cards, personal loans, student loans, and some home improvement loans. *Id.*

261. *Id.* Common examples of secured debts include mortgages and auto loans, which are secured by the home and automobile purchases respectively. *See id.*

262. *Id.*

263. *Id.*

264. *See In re Arehart*, 52 B.R. at 311.

265. *Id.* (finding \$18,856 in unsecured debt); *see also In re Medallion Realty Tr.*, 103 B.R. 8, 9 (Bankr. D. Mass. 1989) (\$300,000 in unsecured debts owed to 100 creditors), *aff'd*, 120 B.R. 245 (D. Mass. 1990).

266. *See infra* note 267.

267. 2 B.R. 332, 335 (Bankr. M.D. Fla. 1980) (“The Court notes that the debtor lists no trade creditors or other debts that customarily result from the conduct of business; the unsecured creditors are principally the accountants and the lawyers.”).

whether a trust is conducting business.²⁶⁸

Secured debt, on the other hand, does not have the same effect.²⁶⁹ A secured loan does not require the same level of trust from the lender because if the borrower defaults on the loan, the lender may repossess the associated collateral.²⁷⁰ In a secured loan situation, the borrower does not have to give the same evidence of profitability as she would for an unsecured loan.²⁷¹ Therefore, secured debt does not point as strongly to an engagement in business as unsecured debt does.²⁷² For example, in *In re Star Trust*, the debt at issue was secured by the properties held by the trust.²⁷³ However, the court found the evidence of secured debt insufficient; thus, the trust was not conducting enough business to be considered a business trust.²⁷⁴ Secured debt, as opposed to unsecured debt, merely shows that the trust was in possession of land.²⁷⁵ Therefore, when evaluating this prong, the court should look to see if the trust has unsecured trade creditors because they serve as considerable evidence that the trust is engaged in sufficient business to be considered a business trust.²⁷⁶

3. Profit-Making Purpose

The third prong of the proposed approach asks the court to evaluate whether the trust instrument shows a profit-making purpose.²⁷⁷ In the precedent on this issue, some courts chose to look at the trust instrument over the current operation of the trust or vice versa.²⁷⁸ However, this proposed test splits up the question and asks the court to evaluate the present operations of the trust and the language in the trust instrument equally.²⁷⁹

A profit-making purpose is central to the business trust: “[M]ost courts

268. See *supra* notes 264–65 and accompanying text.

269. See *supra* note 260 and accompanying text.

270. See *supra* note 260 and accompanying text.

271. See *supra* note 260 and accompanying text.

272. See *In re Star Tr.*, 237 B.R. 827 (Bankr. M.D. Fla. 1999).

273. *Id.* at 831–32.

274. *Id.*

275. See *supra* note 260; see also *In re Star Tr.*, 237 B.R. at 827 (finding the presence of debt secured by trust property insufficient to show business operations).

276. See *In re Treasure Island Land Tr.*, 2 B.R. 332, 335 (Bankr. M.D. Fla. 1980).

277. See *infra* notes 280–81.

278. See *infra* Part IV.C; see also *Morrissey v. Comm’r*, 296 U.S. 344 (1935) (applying the federal income tax definition of a corporation, which requires a general involvement in business—a combination of the factors proposed here).

279. See *infra* Part IV.C.

agree that a basic distinction between a business trust and other trusts is that business trusts are created for the purpose of carrying on some kind of business.²⁸⁰ In *In re Ralph Faber Trust*, a family farmer created a trust with “the express purpose of holding, managing, investing and re-investing the trust property until the death of his last surviving child.”²⁸¹ In holding that the trust was not a business trust, the court relied on the fact that the express purpose of the trust was not for profit but rather to maintain the trust property for the benefit of the farmer’s children.²⁸² The court did not place much weight on the current operation of the trust, which was leasing the land to other farmers for profit.²⁸³ The purpose of the trust was by far the largest factor in the court’s decision.²⁸⁴

While the emphasis on the purpose of the trust was appropriate, in order to analyze the totality of the circumstances the court should have analyzed factors other than the express purpose of the trust. For instance, the trust was engaged in the business of leasing farmlands to other farmers and reaping the profits.²⁸⁵ If a more comprehensive approach, such as the proposed restatement test, was applied, the court would have given the current operations of the trust more weight and potentially found that the trust was engaged in sufficient business.²⁸⁶

Similarly, in *In re Treasure Island Land Trust*, the court reasoned that the powers of the trustee set forth in the trust instrument were “central to [the trust’s] purpose” and of great importance in determining whether the trust is a business trust.²⁸⁷ In concluding that the trust was not a business trust, the court

280. *Shawmut Bank Conn., Nat’l Ass’n LNC Invs., Inc. v. First Fid. Bank (In re Secured Equip. Tr. of E. Air Lines, Inc.)*, 38 F.3d 86, 89 (2d Cir. 1994); see also *In re Visicon S’holders Tr.*, 478 B.R. 292, 308 (Bankr. S.D. Ohio 2012) (“A business trust is ‘created with the primary purpose of transacting business or carrying on commercial activity for the benefit of investors.’ By contrast, trusts ‘designed merely to preserve the trust res for beneficiaries generally are not business trusts.’” (quoting *Brady-Morris v. Schilling (In re Kenneth Allen Knight Tr.)*, 303 F.3d 671, 680 (6th Cir. 2002))); *Merrill v. Allen (In re Universal Clearing House Co.)*, 60 B.R. 985, 991 (Bankr. D. Utah 1986) (“The primary consideration in most cases has been the overt purpose of the trust. If its purpose is to protect the trust res, the trust is found to be ineligible for bankruptcy protection. If the purpose is profit oriented, the trust is found to be an eligible business trust.”).

281. *In re Ralph Faber Tr.*, 113 B.R. 599, 600 (Bankr. D.N.D. 1990).

282. *Id.* at 601 (“The trustee himself testified that the purpose was to ensure the farm’s longevity.”).

283. *Id.*

284. See *id.*

285. *In re Ralph Faber Tr.*, 113 B.R. at 601.

286. See *infra* Part IV.B.4.

287. *In re Treasure Island Land Tr.*, 2 B.R. 332, 334 (Bankr. M.D. Fla. 1980); see also *Merrill v. Allen (In re Universal Clearing House Co.)*, 60 B.R. 985, 992 (Bankr. D. Utah 1986) (“In nearly all

reasoned that the express purpose of the trust was to hold and manage property rather than conduct business.²⁸⁸

Several courts have looked to the intentions of the creators of the trust as evidence that the trust is engaged in business.²⁸⁹ Therefore, an evaluation of the trust instrument, and whether it describes a profit-making purpose, is necessarily included in this proposed restatement approach.

4. Current Business Operations

In addition to analyzing the intended purpose of the trust, it is also important for the court to analyze the current operations of the trust. The proposed restatement test includes both an emphasis on the stated purpose of the trust and the current operations of the trust in order to give the court the most accurate insight possible into whether the trust is engaged in business. Additionally, courts have stressed the importance of evaluating both factors in their determinations.²⁹⁰ Thus, in order to ensure an analysis of the totality of the circumstances, the proposed restatement test asks the court to analyze both the purpose of the trust as well as the current operations of the trust.²⁹¹

The court's analysis in *In re Cohen*, although over-inclusive, provides a good framework for a court's analysis under this prong.²⁹² The *In re Cohen* court underwent a twenty-four-step approach in its determination that a trust was not conducting sufficient business.²⁹³ The test proposed here does not require analysis on the same level; however, the *In re Cohen* court's findings centered on the current business operations of the trust and are helpful to examine in the context of the "current business operations" prong.²⁹⁴ The *In re*

cases, trusts which have been denied status as business trusts under the Bankruptcy Code have been 'simple land trusts' created under trust agreements that strictly limited the authority of the trustees.')

288. *In re Treasure Island Land Tr.*, 2 B.R. at 336.

289. See, e.g., *In re BKC Realty Tr.*, 125 B.R. 65, 68–69 (Bankr. D.N.H. 1991) ("To qualify as a business trust the trust . . . must have been formed primarily for a business purpose."); *In re Ralph Faber Tr.*, 113 B.R. at 599; *Merrill*, 60 B.R. at 985 (finding that the express purpose of the trust was for profit and not merely the management of assets).

290. See *In re Jin Suk Kim Tr.*, 464 B.R. 697, 704 (Bankr. D. Md. 2011) ("The one overriding principle that emerges from the cases is that the determination of whether a trust is a business trust is fact-specific and focuses on the purpose and operations of the trust.')

291. See *In re Star Tr.*, 237 B.R. 827 (Bankr. M.D. Fla. 1999) (concluding that in deciding whether a trust qualifies as a business trust, the focus should be on the totality of the circumstances).

292. 4 B.R. 201 (Bankr. S.D. Fla. 1980).

293. *Id.* at 208–09.

294. *Id.* (applying several factors related to the current operations of the trust, including whether the trust had a place of business and whether it had filed tax returns).

Cohen court found that the trust had not filed separate corporate income tax returns, had no income from operations, and had no office from where to conduct business, if there was any.²⁹⁵ Ultimately, the court found that the trust had little to no current business activity and therefore was not a business trust.²⁹⁶

The court in *In re Mohan Kutty Trust* looked at similar characteristics of a trust in its analysis of the current operations of the trust.²⁹⁷ The court determined that the trust in question was not a business trust because it lacked employees and did “not buy or sell merchandise or render a service.”²⁹⁸ Thus, when analyzing this prong, the court should look to the current operations of the trust and determine whether the trust is currently conducting business by observing whether the trust has filed tax returns, hired employees, filed corporate income tax returns, has income from operations, or buys and sells goods or performs a service.²⁹⁹ These points of observation show a strong indication of current business activities and aid the court in making the proper determination under this final factor.³⁰⁰

C. Sliding Scale

Under the proposed restatement test, a court should analyze all of the factors presented in unison; the strong presence of one makes the presence of the others less necessary.³⁰¹ However, the final two prongs are central to the analyses of several courts and are the weightiest of the proposed factors.³⁰² Thus, the court should apply a sliding scale approach when evaluating the last

295. *Id.* at 203.

296. *Id.*

297. *In re Mohan Kutty Tr.*, 134 B.R. 987, 989 (Bankr. M.D. Fla. 1991).

298. *Id.*

299. This list is not dispositive but merely seeks to provide a general idea of what the court should be looking for in its analysis under this prong.

300. See *In re Mohan Kutty Tr.*, 134 B.R. at 989; *In re Cohen*, 4 B.R. at 201. Both of these cases illustrate the importance of a close analysis of the current operations of the trust.

301. See *infra* note 302 and accompanying text.

302. See *In re Star Tr.*, 237 B.R. 827 (Bankr. M.D. Fla. 1999) (stating the inquiry of the court should be centered around the trust documents and the totality of the circumstances); *In re BKC Realty Tr.*, 125 B.R. 65, 68–69 (Bankr. D.N.H. 1991) (“To qualify as a business trust the trust must not only be [sic] doing business, and have some of the significant attributes of a corporation, but also must have been formed primarily for a business purpose.”); *In re Margaret E. DeHoff Tr. I*, 114 B.R. 189, 191 (Bankr. W.D. Mo. 1990) (considering among other factors whether the trust was “created and maintained for a business purpose” (emphasis added)).

two factors in order to consider the totality of the circumstances.³⁰³ Under such an approach, if the trust has minimal evidence of a profit-making purpose, it could overcome the deficiency by presenting strong evidence of current business operations.³⁰⁴

Previously, when courts have applied the last two prongs, they were in isolation from one another.³⁰⁵ In *In re Gulfcoast Irrevocable Trust*, the court evaluated whether three separate trusts, which took out considerable loans for heavy equipment, were business trusts.³⁰⁶ In making its determination, the court analyzed the purpose of the trust and its current operations in isolation from one another.³⁰⁷ The court established that the trusts were not created to conduct business nor were they involved in sufficient commercial activity.³⁰⁸ Ultimately, the court held that the trusts were not business trusts eligible for bankruptcy protection.³⁰⁹ In that instance, applying the final two factors in isolation did not allow the court to look to the totality of the circumstances but rather forced it to take a segmented view.³¹⁰

Under the proposed approach, the strong presence of current business operations would soften the necessity for a profit-making purpose and vice versa.³¹¹ This approach gives a court leeway to grant bankruptcy protections to trusts that started with the intention of being a business trust but do not have individually sufficient current operations and trusts that were not created as a business trust but do have extensive current business operations.³¹² To provide

303. See *supra* note 302 and accompanying text.

304. See *Davis v. Pension Ben. Guar. Corp.*, 571 F.3d 1288, 1291–92 (D.C. Cir. 2009) (analyzing the application of a sliding scale test).

305. See *In re Gulfcoast Irrevocable Tr.*, No. 12-06338, 2013 WL 6499180, at *2 (Bankr. D.P.R. Dec. 11, 2013).

306. *Id.*

307. *Id.*

308. *Id.* The court reasoned that “[t]he Trusts are merely holding companies of affiliates operating in Puerto Rico.” *Id.* at *4.

309. *Id.*

310. *Id.* If the court were to look at the whole life of the trust using the sliding scale approach, then it would have been more likely to find that the trust was conducting sufficient business because it would have taken more factors into account.

311. See *Davis v. Pension Ben. Guar. Corp.*, 571 F.3d 1288, 1291–92 (D.C. Cir. 2009) (“If the movant makes an unusually strong showing on one of the factors, then it does not necessarily have to make as strong a showing on another factor.”). Here, the circuit court is evaluating the use of a sliding scale in the context of a preliminary injunction. *Id.* However, the principles are the same: if, under the proposed test, the debtor makes a strong showing under the profit-making purpose factor, it does not have to make as strong a showing under the current business operations prong.

312. See *supra* Part IV.B.3–4 (describing the importance of analyzing both the initial purpose of the trust as well as the current operations of the trust to view the whole life of the trust).

a more holistic analysis, a court should apply the last two prongs in unison using a sliding scale, thereby evaluating the totality of the circumstances, not the trust's creation or current operations in isolation from one another.³¹³

V. CONCLUSION

The current state of the law regarding the business trust in bankruptcy is hopelessly confused.³¹⁴ Courts have applied tests ranging from twenty-four factors³¹⁵ to an application of federal income tax law to determine when a trust is a business trust.³¹⁶ However, throughout the history of the business trust, there have been several factors that have remained constant: (1) the trustee must be the “master” of the trust property, (2) there must be limited liability for the trustee, (3) the business trust is similar yet distinct from a corporation, and (4) the main objective of the trust is the operation of business.³¹⁷ The four factors proposed in this Comment—(1) voluntary pooling of capital with freely transferable shares, (2) presence of creditors, (3) profit-making purpose, and (4) current business operations—are aimed at maintaining consistency with the history of the business trust and providing bankruptcy courts with a uniform test.³¹⁸ This uniform test will fulfill Congress's goal to avoid a “patchwork of different bankruptcy laws” by allowing the application of a consistent predictable approach while also curing the confusion that plagues the courts.³¹⁹

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313. In evaluating the final two prongs, the court is required to look to the genesis of the trust as well as its current operations, supplying the court with the most detailed picture possible. *See supra* Part IV.B.3–4.

314. *See supra* Part III.B.2.

315. *In re Cohen*, 4 B.R. 201, 203–04 (Bankr. S.D. Fla. 1980).

316. *Morrissey v. Comm’r*, 296 U.S. 344 (1935); *see also Mosby v. Boatmen’s Bank of St. Louis Cty. (In re Mosby)*, 61 B.R. 636 (E.D. Mo. 1985) (applying the same test based on federal income tax law).

317. *See supra* Part II.

318. *See supra* Part IV.B.

319. Austin, *supra* note 201, at 1152.

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