INSTITUTIONALIZED TRUSTEESHIP: AVENUES OF COMPENSATION REFORM

The trust function of providing security for life beneficiaries has, in recent years, vastly overshadowed the function of trusts as a conduit for the transmittal of family fortunes to remaindermen. As both interest rates and purchasing power have declined, the demand for active and expert supervision of trust investments has become intensified. To assure such supervision, an increasing number of settlors are employing banks and other corporate institutions as their trustees. This trend, coupled with the willingness, indeed aspiration, of corporate fiduciaries to serve, has resulted in their phenomenal increase in size and number during the past fifty years.

1. See Bardt, Trust Management Static or Dynamic, 28 Trust Bull. 2, 4 (Dec. 1948); Stone, Life Tenant vs. Remainderman, 84 Trusts & Estates 530, 531 (1947). For the traditional view espousing the custodial functions, see Headley, Trustees or "Gentlemen Adventurers?" 88 Trusts & Estates 91 (1949).


3. All but approximately 100 of the 2976 trust institutions are either banks with trust departments or trust companies with banking departments. Stephenson, Trust Business in the United States, 1947, 27 Trust Bull. 19, 20 (Apr. 1948). For the sake of convenience, the descriptive term "trust department" will occasionally be used where the principles being discussed are applicable to all trust institutions.

4. There was a time when trustees were not looked upon kindly if they thrust themselves forward rather than await selection. See May v. May, 167 U.S. 310, 322 (1897); Sears, A Treatise on Trust Co. Law §13 (1917). However, extensive promotional activities are now a well established practice of trust institutions. See Stephenson, Trust Advertising, 28 Trust Bull. 19 (Jan. 1949); Weldon, New Business for the Trust Department (1933). Lawyers have been particularly critical of this so-called "will chasing." See, e.g., Johnson, The Unfair Competition of Trust Companies, 22 Can. B. Rev. 422 (1944). Several states have responded by regulating the solicitation of fiduciary appointments. Ark. Stat. Ann. 571 (Pope, Cum. Supp. 1944); N.H. Rev. Laws, c. 312, §13 (1942); Wash. Rev. Stat. §3231(9)* (Remington, 1932); cf. 32 Mass. L.Q. 14 (1947) (memorandum on one of the half dozen bills proposed in Massachusetts).

5. In 1895 there were an estimated 569 trust companies with total resources in excess of $962,000,000. Perine, Statement of the Growth and Present Status of Trust Companies in the United States (1905) (unpaginated reprint of address before Trust Company Section of A.B.A.). In 1947, 2976 companies controlled $36,162,161,448 of personal trust property. Stephenson, Trust Business in the United States, 1947, 27 Trust Bull. 19, 21 (Apr. 1948); 86 Trusts & Estates 206 (1948). The number of companies has dropped since the peak in the 1920's. Drake, Thirty Years Back and a Look Ahead in Trust Administration, 79 Trusts & Estates 555,556 (1944); see Lee, Personal Trust Administration 1 (1934). But there has been a significant gain in assets particularly since 1941. See American Bankers Association, Present Day Banking, 1947-1948 195 (Kuhns ed. 1947) (cited hereafter as Present Day Banking).
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The corporate trustee has little in common with the old-line fiduciary, who was content with an honorarium awarded under a rule-of-thumb system as his material return. The new-style fiduciary is understandably impelled by the profit motive. Yet the service of corporate trustees should be available to beneficiaries at the lowest reasonable price. These conflicting interests can be fairly reconciled only if the system of compensation is geared to the cost of doing business. Since the current system is not, new methods of reimbursing trustees should be examined.

EVOLUTION OF THE CORPORATE TRUSTEE

Testators and settlors, while cognizant of the many merits of individual fiduciaries, early recognized the desirability of securing continuous trusteeship. Colonial probate records are interspersed with numerous instances in which several co-executors were appointed to administer an estate or in which the church was requested to fulfill this function. A forecast of future development came at the end of the 18th Century when trustees for private funds devoted to specific limited purposes were first incorporated. The embryo of the modern corporate fiduciary, however, did not develop until 1818, when the Massachusetts Hospital Life Insurance Company began to perform specialized trust service. In the following two decades, marked

6. No attempt will be made here to weigh the arguments concerning the advantages of the corporate over the individual trustee. The following have been the principle advantages claimed: permanency, protective facilities, experience and specialization, financial responsibility, collective knowledge and judgment, and extra-judicial government supervision. See STEPHENSON, THE AMERICAN SYSTEM OF TRUST BUSINESS 15-9 (1936); Jour- ney, Are You Missing Trust Business? 41 BANKING 40, 41 (Oct. 1948). An extremely critical approach is taken by KELLY, HOW TO LOSE YOUR MONEY PRUDENTLY (1933) passim. See the debate between Leverett Saltonstall, speaking for the professional individual trustee, and Frederick A. Carroll, representing the professional corporate trustee, in Is There a Field for the Professional Trustee, 67 TRUST Co. 136 (1938).

7. SMITH, THE DEVELOPMENT OF TRUST COMPANIES IN THE UNITED STATES (1923) (cited hereafter as SMITH) contains the best account of the corporate trustee's early growth. In addition, see STEPHENSON, TRUST BUSINESS IN COMMON LAW COUNTRIES 538-40 (1940); HERRICK, TRUST COMPANIES c. 1 (2d ed. 1915).

8. George Washington, for example, appointed seven executor-trustees ranging from 19 to 68 years in age. The youngest member of the group closed out the estate after a 51 year administration. Prussing, George Washington as Real Father of the Modern Trust Company, 45 TRUST Co. 423 (1927).


10. SMITH 234. Early common law forbade a corporation to act as a trustee. But the legal path was cleared by Attorney General v. Landerfield, 9 Mod. 226, 83 Eng. Rep. 456 (Ch. 1743); Vidal v. Girard's Executors, 2 How. 126 (U.S. 1844); Trustees of Phillips Academy v. King, 12 Tyng 545 (Mass. 1816).

11. The Company's directors assumed the authority to accept trusts from general clauses in their charter. SMITH 239-40. The first corporation ever specifically granted trust powers was the Farmers' Fire Insurance and Loan Company (now City Bank Farmers Trust Co. of New York City) in 1822. Id. at 246. The first trust business of record was a guardianship in 1831. STEPHENSON, THE AMERICAN SYSTEM OF TRUST BUSINESS
as they were by the spectacular growth of urban communities, liquid wealth, and millionaires, the corporate trustee emerged as a recognized institution.

Although considered incidental to such activities as title abstracting and life, fire and marine insurance, the early trust business was apparently profitable. Prior to 1850, trust funds were usually thought of as funds upon which the company paid contractual rates of interest, retaining for its service all sums earned in excess of that rate. This business was supplemented by trust funds in the modern sense—funds invested for the sole gain of beneficiaries with the trustee's compensation limited to a set fee.

But the pattern of corporate trusteeship was not yet fixed. Financial conditions after 1850 progressively favored the assumption of trust business by banking institutions. The panic of 1857 resulted in new capital adjustments requiring employment of trustees under bond issues at the very time when banking was evolving into a national system. The expansion of utilities, corporate organization of businesses and government financing incident to the Civil War increased personal investment opportunities and problems. With the development of the mutual principle in life insurance and the accompanying abandonment of collateral trust business, the field was cleared for banker trust companies. Accepting the opportunity to undertake corporate and personal trust services, trust departments expanded rapidly until in 1905 they controlled resources of over 4 billion dollars—1/10 of the world's aggregate banking power. And in

9–10 (1936). This was followed by a living and a testamentary trust (1835), an administratorship and an executorship (1839), and a trusteeship under a corporate bond issue (1839). Id. at 9–11. See PERINE, THE STORY OF THE TRUST COMPANIES (1916).

12. STEPHENSON, TRUST BUSINESS IN COMMON LAW COUNTRIES 539–40 (1940).

13. SMITH 281–2; AMERICAN INSTITUTE OF BANKING, TRUST FUNCTIONS 15, 16 (1927) (cited hereafter as TRUST FUNCTIONS). A few companies today have reversed this process; they conduct insurance, abstracting and loan business collateral to their trust functions.


15. SMITH 316; STEPHENSON, THE AMERICAN SYSTEM OF TRUST BUSINESS 10 (1936).

16. SMITH 281, 316.

17. Id. at 284.

18. Id. at 287; REMINGTON, op. cit. supra note 13, at 35–6; HERRICK, op. cit. supra note 7, at 10–2, 16–9.

19. Although this process was substantially completed by 1890, SMITH 288, the last of the trust insurance companies did not separate its activities until 1922 when the Provident Life and Trust Co. of Philadelphia split into the Provident Mutual Life Insurance Co. and the Provident Trust Co. STEPHENSON, TRUST BUSINESS IN COMMON LAW COUNTRIES 543 (1940).

The association of trust with banking activities evoked some criticism in the early 1930's but is apparently unquestioned today. The arguments for and against dissociation are presented in REMINGTON, op. cit. supra note 13, at 63–83.

20. PERINE, STATEMENT OF THE GROWTH AND PRESENT STATUS OF TRUST COMPANIES IN THE UNITED STATES (1905). As many new trust companies were organized from 1899 to 1905 as had been formed during the entire preceding three-quarters of a century. The total trust assets in the 1,547 companies then in existence exceeded the total of life insurance assets by $1,300,000,000 and the total resources of savings banks by $500,000,000.
1913 the available trust facilities were materially expanded by adoption of the Federal Reserve Act which authorized national banks to participate in these trust activities for the first time.

Once established, the corporate trustee found an expanding market for its services. The initial incentive for employment of the trust over other investment devices was provided by tax advantages. In addition, Liberty Bond drives and prosperity soon combined to make the public investment-conscious. In 1912, bonds were being shunned by investors as yielding too little income at 4 to 5%, while corporate obligations were not generally

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*Ibid.* The major portion of this expansion was attributable to corporate rather than personal trust services. Remington, *op. cit. supra* note 13, at 37-8. This may tend to explain the 1903 profit of $17,383,608 earned by 81 New York trust companies. Kilburn, *Control and Supervision of Trust Companies*, 24 *Annals* 29, 34-5 (1904).


22. State banks and trust companies waged a bitter fight to prevent the national banks' acquisition of fiduciary powers. Remington, *op. cit. supra* note 13, at 37. Spurred by the serious inroads on the loan and deposit field which were attributed to the lack of uniformity in the regulation of state institutions possessing charters containing broad grants of power, national banks conducted a vigorous counter-campaign to secure fiduciary powers for themselves. See Neilan, *Trust Examination* 14 (1939). The accompanying attempt to obtain more effective trust company supervision is discussed *id. passim.* Even after the initial grant of trust powers in 1913, the national banks were frequently inhibited in their exercise of such powers by state laws. In 1918, an amendment to the Federal Reserve Act removed the possibility of discriminatory legislation by gearing the national banks' fiduciary powers to the like powers exercised by their state competitors under local law. 40 *Stat.* 968 (1918), 12 *U.S.C.* § 248(k) (1946). These Congressional grants of trust authority were upheld by the courts. Missouri *ex rel.* Burns Nat. Bank v. Duncan, 236 *U.S.* 17 (1924); First Nat. Bank v. Fellows *ex rel.* Union Trust Co., 244 *U.S.* 416 (1917); see Hamilton v. State, 94 Conn. 648, 110 *Atl.* 54 (1920). See, generally, Stephenson, *The American System of Trust Business* 11, 12 (1936). Of the 2,976 trust institutions, 48% are now national banks, doing 31.7% of the country's trust business. Stephenson, *Trust Business in the United States*, 1947, 27 *Trust Bull.* 19, 26-7 (Apr. 1948). See *Trust Functions* 17 (1927).

The major functions of the corporate fiduciary—trusteeships for individuals under will and for individuals and corporations under agreement, executorships, guardianships and custodial and agency arrangements—were well established by the time national banks entered the field. See Sears, *op. cit. supra* note 4, at § 3. Since then, major additions to functions have come in the administration of life insurance trusts, Hixson, *Life Insurance Trusts* (1933), community trusts, Loomis, *New Development in Community Trusts*, 81 *Trusts & Estates* 203 (1945), and employees' trusts, Goldstein, *What is New in Organizing, Amending and Operating Your Pension and Profit-Sharing Trusts?* 6 *Inst. Fed. Tax.* 903 (1948); 86 *Trusts & Estates* 41 (1948).

23. While this continues to be an inducement, see Schwalm, *Trust Service at a Profit*, 84 *Trusts & Estates* 631, 632 (1947), its importance is being considerably reduced in the income tax field, see Note, *Irrevocable Trusts and the Federal Income Tax*, 49 *Yale L.J.* 1305 (1940), and *Int. Rev. Code* § 51(b) (all married taxpayers may split their income for tax purposes), and, to a lesser extent, in the estate tax field. See Bithler, *The Church and Spiegel Cases: Section 211(c) Gets a New Lease of Life*, 58 *Yale L.J.* 825 (1949).

favored; three-quarters of trust assets were invested in mortgages, with the balance in real estate and stocks in real estate companies. In the 1920's, however, investment practices broke from this pattern and developed into the sharply contrasting pattern of today, when well over 90% of all trust investments consist of stocks and bonds. Settlers recognized that these investments require more experienced judgment and administrative attention than the predominately mortgage investments of yesteryear. Moreover, as income, inheritance and personal property taxation grew more and more complex, the services of the corporate trustee as an expert collectively in law, accounting and business trends became more and more attractive.

The increased expense which accompanied the new complexity of trust business was alone enough to cause professional trustmen to question whether their return was worth the capital they had invested. But in addition, trust companies have been squeezed by a rare combination of events in the past 20 years. During the last depression, beneficiaries who had been clamoring for extensive investment activity from their fiduciaries now resorted to the courts for recovery of principal depleted through loose investment practices. The courts responded by holding the trustees to high standards of fidelity, under penalty of heavy surcharge. At the same time, falling interest and dividend rates produced a marked decrease in the trust income on which trustee’s fees were largely based. Furthermore, interest and dividend rates have not yet regained the peak level of the twenties, while costs have risen with the general level of prices.

Professional trustees have been unable to determine true profit and loss statistics due to the absence of cost accounting systems. Nevertheless, they have allowed their apprehension that trusteeship was unprofitable to ripen into a conviction. Many banks have closed their trust departments. Others have rationalized that the cash loss in the trust department was out-

25. See Drake, supra note 5, at 555. For a case study of the investments in a selected group of trusts, see Riddle, The Investment Policy of Trust Institutions c.c. 9-19 (1934). Trends from 1919 to 1932 in the diversification of real estate, bonds and stocks are noted id. at 159-60, 173-4.


27. See note 6 supra. For an analysis of the functional details of the tax division in a modern trust department, see Williams, The Tax Division of a Trust Department (1949) passim (mimeographed).

It is also likely that the greater responsibility being imposed by law and closer supervision by courts and banking authorities led informed individuals to employ the corporate in preference to the individual trustee. See, generally, Kilburn, supra note 20; Neilan, Trust Examination (1939).

28. See Moore, A Rationalization of Trust Surcharge Cases, 96 U. of Pa. L. Rev. 647 (1948), and the cases collected therein.

29. See note 2 supra and p. 931 infra.

30. See pp. 949-51 infra.

31. Drake supra note 5, at 556; Steber, Should Small Banks Have Trust Departments? 88 Trusts & Estates 98 (1949), 28 Trust Bull. 3 (April 1949) (1948 survey revealing that 10% of Pennsylvania's trust departments were closed or closing).
weighed by indirect benefits such as the creation of good will for the banking institution as a whole. The majority, however, has instituted a concerted movement to increase rates of compensation. Results of the limited investigations which have been conducted are substantially of one tenor—the personal trust business as a whole is being carried at a loss, with only a few trustees able to maintain the volume of large trusts necessary to achieve a profit under traditional methods and rates of compensation.

The implications of these disclosures are significant for the future of private trusteeship. If small trusts are to be rejected because unprofitable, trustees will find themselves riding the ebbing tide of large fortunes. And if a substantial number of trusts are saddled with costs disproportionate to benefits, either settlors and beneficiaries will be denied the use of the trust device or legislators will be forced to consider some form of public trusteeship as the means for attaining reasonably priced fiduciary services. Both

32. See Rockwell, Ascertaining Cost as Basis of Fair Compensation for Trust Service, 45 TRUST Co. 283, 284 (1927). Securing checking and savings accounts, selling bonds or mortgages to the client and depositing funds awaiting investment in the banking department were some of the additional benefits stressed. Ibid. And see 27 TRUST BULL 13 (Sept. 1947): While trust earnings are small in comparison to total bank profits, they are not subject to fluctuation in deposits or employment of capital and are thus a factor in the bank's stability.

33. The Trust Division of the American Bankers Association, in combination with local fiduciary groups, provides the organization through which changes are sought. See Theis, History of Trust Cost Accounting, 18 TRUST BULL 23, 24 (Oct. 1938).

34. In 1943, New York's State Banking Department undertook an official study of trust department earnings and expenses. "The study established the fact that corporate fiduciaries as a group were losing money on their personal trust business and that consequently trust departments of banks were not making a proper contribution toward the upbuilding of capital funds." ANN. REP. SUP. OF BANKS 6 (N.Y. 1944). The report is summarized in 76 TRUSTS & ESTATES 347 (1943); id. at 451; id. at 529; 22 TRUST BULL 13 (June 1943). While this has been the only investigation by a state supervisory authority, the Federal Reserve Bank of Boston has also pioneered in official investigation, though on a more limited scale. See Hoyle, New Trust Cost Analysis, 57 TRUSTS & ESTATES 171 (1948).

Unofficial statewide studies have been made by banking groups in several states. See Weig, Trust Costs—A Guide to Trust Fees, 25 TRUST BULL 3, 4-5 (May 1946); 24 TRUST BULL 18 (Sept. 1944) (summarizing findings in New Hampshire); Wilson, Pennsylvania's Third Trust-Cost Survey, 21 TRUST BULL 17 (July-Aug. 1942).

"Generally speaking, the[se] studies showed that corporate trust business was operating on a profitable basis and that fees for executorships and administratorships showed a satisfactory profit. The difficulty lay in the cost of administering trusts under will, trusts under agreement and agency accounts." Lowell, supra note 2, at 17.

35. State-operated trust business has been extensively developed in a number of civil and common law countries. See Stephenson, Studies in Trust Business c. 16 (1st series 1938); STEPHENSON, TRUST BUSINESS IN COMMON LAW COUNTRIES (1940) passim; REMINGTON, op. cit. supra note 13, at 21-30. HEANEY, PUBLIC TRUSTEESHIP (1942) discusses the office of public trustee in England and New Zealand. The pioneering work of the latter country is particularly significant: a judicious combination of public trusteeship, common trust funds and state guarantee of both principal and income has been of especial economic and social value to the administration of small accounts. Specifically, the office has become an experimental clinic for the improvement of trust law and pro-
the trustman and the trust user are thus notably interested in possibilities of compensation reform.

TRADITIONAL PATTERN OF COMPENSATION

The United States early rejected the English common law notion of honorary trusteeships, under which remuneration was forbidden lest the trustee overload the trust with costs and precipitate contention as to the value of his services. Rather, in this country, the theory developed that the amount of compensation is open to negotiation between the settlor and trustee.

In addition, beneficiaries are allowed to remunerate the trustee and their contract to that effect is enforced.

Absent any such provision by the parties, a trustee is entitled to the procedure through such innovations as low cost legal counsel and a near-minimum of reference to the courts, investment and managerial practices have been refined, id. at 107, and the unmatched continuity and security of the state has been a factor in the popularity of the office's services. Id. at 111. Moreover, New Zealand's public trustee provides an ideal agency for the management of a number of different kinds of public and quasi-public funds, id. at 107.

In this country, the germ of public trusteeship exists in about half the states in the form of a public administrator for certain intestate estates. See Stephenson, Studies in Trust Business 241-2 (1st series 1938). Whether this rudimentary beginning will ripen into public trusteeship may depend on the success of privately conducted common trust funds. See pp. 933-40 infra. Cf. Jacobs & Cahn, The Fiduciary of the Future, 5 Johns L. Rev. 32, 41 (1930), advocating the transformation of American trust companies into public trustees as a step toward compelling settlors to select fitting fiduciaries to administer trust funds. Some of the practical questions which would have to be met if public trusteeship is adopted in the United States, are raised by Heaney, op. cit. supra, at 109-13.


The general American rule allowing the trustee a reasonable profit applies in both testamentary and inter vivos trusteeships. Illinois is the major exception. Like a number of other states, e.g., Walton v. Gairdner, 111 Ga. 343, 36 S.E. 666 (1900), Illinois holds that the right to compensation is purely statutory. Cook v. Gilmore, 133 Ill. 139, 24 N.E. 524 (1890). Since the Illinois statute granting reasonable compensation does not include inter vivos trustees, they are denied compensation unless the trust instrument provides otherwise. Bennett v. Weber, 323 Ill. 283, 154 N.E. 105 (1926).

37.() 4 Bogert, The Law of Trusts and Trustees § 975 (1948); 2 Scott, The Law of Trusts § 242.4 (1939) (cited hereafter as Bogert and Scott respectively). This may in fact be a one-sided privilege weighed in favor of the trustee: attempts by the settlor to avoid by stipulation what he believes to be a harsh statutory levy are frequently negated by the courts and statutes permitting the trustee to elect the statutory fee. See Comment, Compensation of Fiduciaries, 42 Yale L.J. 771, 773-8 (1933); Note, 161 A.L.R. 870 (1946).

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compensation prescribed by the legislature or the court. If there is no controlling statute, the trustee is guaranteed compensation which is judicially "reasonable." Where a statute covers the matter, it either expressly directs the court to make a discretionary award of "reasonable" compensation, or it sets out a schedule to be followed in all cases.

The usual practice has been to compute the income commission, the major portion of the fee, on the basis of an agreed or statutory percentage of the trust income, the theory being that this constitutes reimbursement for current expenses. In many states, this percentage is graduated downward as the size of the trust increases. The lesser part of the trustee's compensation, the principal commission, is intended to constitute a reasonable margin of profit. Traditionally, this has been levied only at the termination of the trust or the particular trustee's duties, regardless of their duration.


Compensation for national banks is governed by the law of the state in which they are located. 12 Code Fed. Regs. § 206.14 (1933). If there is no state regulation on the subject and no provision in the instrument, reasonable compensation is assured. Ibid.

40. E.g., Ill. Stat. Ann. c. 148, § 31 (Smith-Hurd, 1936); Pa. Stat. Ann. tit. 20, § 3271 (Purdon, 1936) (see note 36 supra); cf. Maine Rev. Stat. c. 140, § 44 (1944) (placing a maximum limit on the court's discretion); Mass. Gen. Laws c. 206, § 16 (1932) (reasonable basis applies to all fiduciary duties). The Montana statute distinguishes between testamentary trustees and trustees under a declaration of trust. The former are granted "reasonable compensation." Mont. Rev. Code § 10353 (1935). The latter are given fees in accordance with the statutory schedule for executors if the instrument is silent, reasonable compensation if the instrument directs that compensation be given without setting the rate, and the trust instrument rate if one has been specified. Id. at § 7918. The state statutes on both executors and trustees compensation are collected in Comment, Compensation of Fiduciaries, 42 Yale L. J. 771 (1933).


42. See 2 Scott 1268-70.

43. 2 Scott 1384. This is particularly true of contractual schedules. See White, New Trends in Trust Compensation, 28 Trust Bull. 13, 25-9 (Oct. 1948). Statutes also recognize, through graduated rates, the fact that costs do not generally increase in proportion to trust size. E.g., N.Y. Sure. Court Act § 285-a (6% on the first $2000 of annual income, 3% on the next $10,000, and 2% on the balance). But cf., Ky. Rev. Stat. § 326.180 (Baldwin, 1943). And where the fiduciary operates under a reasonable compensation doctrine, the size of the estate will be considered as a factor in awarding the total commission, see In re Harrison's Estate, 217 Pa. 207, 209, 66 Atl. 354, 355 (1907), although the actual award may not be computed on a graduated scale. In re Gardner's Estate, 333 Pa. 229, 185 Atl. 894 (1936).

44. "It is the compensation on principal at the termination of the trust which is supposed to wipe out the loss in carrying the account through the years and give the trustee a fair profit." Present Day Banking 194. There is usually no principal compensation where the trust is perpetual. See Drueing, Fees for Charitable Trusts, 83 Trusts & Estates 239 (1946).

Because these traditional measures of compensation bear no direct relationship to costs or to the skill and responsibility of the trustee, many beneficiaries are undoubtedly paying for services never received while contributing toward services rendered to others. At the same time, the relatively burdensome expense discourages trustees from assuming duties in trusts of less than $25,000, thereby largely depriving the moderate income class of the benefits of modern trust methods. Moreover, the frequently unprofitable status of their personal trust business as a whole tends to cause the companies to saddle other fiduciary activities or other divisions of the bank with unjustifiable costs.

Conforming Compensation to Services

Approaching the problem through costs

The increased expense of trust work, and the high variance in cost with each trust, have recently led to experimentation with new devices for giving trustees deserved compensation, while at the same time protecting settlors and beneficiaries from unjust charges.

Size as a cost factor. The availability of institutionalized trusteeship to the small trust is a matter of vital concern to both settlors and trust companies. The need for trust services is unrelated to size: the beneficiary of a small estate may be fully as unfit for the management of the property on which he is dependent as the beneficiary of a large trust. And, in this era of small estates, the trust companies may lose out in the competition for the

( guardianship ); see Bridgeport-City Trust Co. v. First Nat. Bank & Trust Co., 124 Conn. 472, 477–8, 200 Atl. 809, 811 (1938). See note 162 infra.

46. See, e.g., Drake, supra note 5, at 559; Heaney, op. cit. supra note 35, at 108. A recent national survey showed 54% of 144,081 trusts handled by corporate fiduciaries had an annual income of less than $1200. 27 Trust Bull. 3, 4 (Sept. 1947). These statistics would seem to indicate that trustmen as a whole are sympathetic toward the management of small trusts. The fact is, however, that, whether they like it or not, trust companies cannot control the accumulation of numerous unprofitable accounts which is due to the creation of a number of small trusts out of a large testate estate, the split of a large trust during distribution, or the acceptance of small accounts where business pressures intervene. See Stephenson, Studies in Trust Business 309 (1st series 1938). The further fact that most if not all the trust companies actively soliciting small accounts are those with common trust funds, Stephenson, Taking Trust Service to the People, 27 Trust Bull. 37, 50 (Nov. 1947), tends to corroborate the general view that trustmen as a whole are reluctant to administer small trusts.

Certainly, the surface has hardly been scratched in the development of a market for corporate fiduciary services to the moderate income class. One survey indicates that only 6% of the probated estates between $5,000 and $10,000 are going to the corporate trustees. Schwalm, Trust Service at a Profit, 84 Trusts & Estates 631, 632 (1947) (large Indiana county). And in some localities, not over 25% of even the more substantial estates are settled by trust institutions. Present Day Banking 195; cf. 80 Trusts & Estates 7 (1945).

47. See note 34 supra.

only substantial source of personal savings unless they meet the need for trusteeship by selling their fiduciary services to the moderate investor.\textsuperscript{42}

But the management of small trusts is an inefficient and expensive service. Not only is the beneficiary of a $25,000 fund unable to reap the investment advantages accruing to his $250,000 counterpart, but the administrative costs of the smaller trust are about four times as great per $1000 of corpus.\textsuperscript{43}

Consequently, the corporate trustee must either charge a very high proportionate fee in order to cover costs or else render only a perfunctory service limited largely to investment in government bonds.\textsuperscript{44}

Graduation of compensation rates downward as the trust principal and income increase is a partial recognition by courts and legislatures of the fact that large trusts cost proportionately less to administer than do small ones.\textsuperscript{45} But if this principle were carried to the point where a trustee could recoup the cost of every trust, small trusts could not bear the burden of expense. Only an attack on the problems of efficiency and cost will make graduated rates practicable.

Insurance companies and savings banks built their business on the efficient handling of small accounts through mass investment.\textsuperscript{46} The use of this technique was denied to trust companies by the common law prohibition against commingling trust funds.\textsuperscript{47} And when a few corporate trustees experimented with commingled funds under contractual arrangements with settlors, the funds were promptly declared associations subject to taxation at the corporate rate.\textsuperscript{48}

Congress removed this tax barrier in 1936, however, by exempting all

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49. See Headley, Day after Tomorrow In Trusteeship, 89 TRUSTS & ESTATES 9, 12-3 (1945). Williams, Modern Concept of the Trust Device, 28 TRUST BULL. 10, 11-4 (Nov. 1948), lists as the major competitors the purveyors of pure savings service such as banks, building and loan associations and the United States Government, the insurance companies (particularly through life insurance options) and investment bankers and brokers.

50. See Stephenson, Administering Small Trusts, 25 TRUST BULL. 25, 30-1 (Nov. 1945). But see the tempering factors mentioned by Bardt, Expanding Horizons for Trust Business, 79 TRUSTS & ESTATES 537, 538 (1944) (larger estates generate major problems in taxation, accounting, investment and real estate management), and Lasseter, Taking Guesswork Out of Trust Costs, 85 TRUSTS & ESTATES 57, 123 (1947) (some accounts with a minimum fee of $25 prove profitable where there is little activity).

51. See Heaney, op. cit. supra note 35, at 108; Riddle, op. cit. supra note 25, at 44.

52. See note 50 supra.

53. STEPHENSON, STUDIES IN TRUST BUSINESS 260-2 (1st series 1938). Australia, New Zealand, Denmark and Norway are among the countries which have applied this approach to the management of fiduciary funds. Ibid.

54. See, e.g., Doud v. Holmes, 64 N.Y. 635 (1875). The strict prohibition against mingling personal funds with trust funds was extended to require the separate "earmarking" of the investments of each trust. See Legislation, 37 Col. L. Rev. 1384, 1385 (1937).

common trust funds from corporate taxes where they were maintained by a bank exclusively for the investment of fiduciary funds and in conformity with regulations to be established by the Federal Reserve Board. Tying the tax exemption to the Board's regulation assured uniform control over the development of all common funds, whether established in state or national institutions. But in the absence of contractual permission for commingling, neither state nor national banks can use the device unless there is also a state enabling statute. Some seventeen states and the District of Columbia have yet to pass such acts.

Although the practice is now rare, settlors may themselves authorize participation in a common trust fund, except in the few states which explicitly prohibit such funds. These so-called "contract funds" are either "legal," in that they confine the investment power of the trustee to securities on a "legal list" established by statute, or, more usually, "discre-
tionary,” in that they grant discretionary powers allowing a far broader choice of investments. Ordinary, however, common trust funds are set up under the authority of enabling statutes. Like contract funds, these statutory funds may be confined by statute either to securities on the legal list or to securities appropriate for investment by each participating trust’s instrument. The legal-discretionary distinction, however, is non-existent in states following the “prudent man” investment rule, which prescribes discretionary investment.

Major advances in internal trust management have been made possible by the common trust funds for general investment permitted under the Board’s regulation. Ordinarily established by declaration of trust, the fund exists as an entity separate from both the trustee’s assets and the participating estates. Although legal title to the corpus is held by the company as trustee, each participating fiduciary account owns a propor-

63. See id. at 12, 20-1. Difficulties which a draftsman must face when drawing the investment clause of a trust are discussed in Comment, Trust Investment Clauses: A Problem for Draftsmen, 58 Yale L. J. 283 (1949). General considerations in the choice of investment power are taken up in id. at 289–91.
64. Common Trust Funds 12.
65. States where the “prudent man” rule is in effect are listed in Comment, 58 Yale L.J. 288, 292 n.14 (1949).

Special provision is also made for common trust funds invested primarily in real estate mortgages. 12 Code Fed. Regs. § 206.17(d) (Cum. Supp. 1944). While state-sanctioned mortgage participation was an important investment technique before the Board authorized common funds, see Comment, Participation Mortgages as a Method of Trust Investment by Corporate Fiduciaries, 45 Yale L.J. 857 (1936), the depression experience was unfavorable, see Note, 34 Col. L. Rev. 663, 667–74 (1934), and, so far as is known, no mortgage participations have been established under the Board’s regulation. Common Trust Funds 22.

67. Earlier formal devices for establishing the funds are discussed in Legislation, Commingled Investment by Corporate Fiduciaries in Pennsylvania, 87 U. Pa. L. Rev. 577, 590–2 (1939), and Rovner, op. cit. infra note 25, at 47–50. Instructions on drafting the plans used since the Board’s regulation are contained in Common Trust Funds e.4.
68. See Matter of Bank of New York, 189 Misc. 459, 463, 67 N.Y.S.2d 444, 447 (Surr. Ct. 1946) (common fund accounting action): “A new agency for aggregating multiple interests was created and regulated and shares in it were made lawful for investment by trustees. This concept of the common trust fund requires the court to deal with such a fund as an entity separate from the trustee and separate from the individual estates whose moneys are invested in participations in the fund.”
tionate equitable interest and enjoys the benefits or suffers the losses rat-
ably.\textsuperscript{69} No individual trust may have an interest in excess of $50,000 or
10% of the fund, whichever is less.\textsuperscript{70}

Benefits accruing to beneficiaries of the small trust through participation
in a commingled fund can hardly be overemphasized. The high degree of
supervision necessitated by the Federal Reserve Board's regulations\textsuperscript{71} and
allowed by the efficiencies accompanying mass investment permits far
greater diversification\textsuperscript{72} and the judicious timing of purchases and sales.\textsuperscript{73}
Moreover, periodic distributions of principal can now be made without the
necessity for keeping considerable amounts of uninvested assets on hand.\textsuperscript{74}

69. \textit{Common Trust Funds}\textsuperscript{24}.

70. 12 \textit{Code Fed. Regs.} § 206.17 (c) (5) (Supp. 1945). For the interpretation where
a settlor has created more than one trust, see 34 \textit{Fed. Res. Bull.} 1113 (1948).

At establishment of the fund, an initial valuation of the assets is made and “units of
participation” defined on this basis. The majority of trustees have initially valued each
unit at $10. The value of a unit at any time thereafter is its proportionate part in the
value of the whole fund. See \textit{Common Trust Funds}\textsuperscript{26}. No additions or withdrawals
are permitted until one of the periodic valuation dates. 12 \textit{Code Fed. Regs.} § 206.17
(c) (Supp. 1945). It is not necessary that the entire assets of a participating trust be
invested in the fund and in fact they are not in many cases. Ward, \textit{The Rise of Common
Trust Funds}, 34 \textit{Banking} 32, 82 (Nov. 1941). Thus, within the maximum participating
limits, large trusts may enjoy the benefits of common trust funds.

71. \textit{E.g.}, quarterly valuations of the fund's assets, prompt segregation of all invest-
ments which become ineligible, complete review of all investments to determine safety and
current value at least once every twelve months, review of all investments to determine
their eligibility for each trust whenever a participant withdraws. See the detailed specifi-
cation of duties in \textit{Common Trust Funds}\textsuperscript{44-8}.

72. Forty-three institutions reporting to the American Bankers Association revealed
the following diversification record on commingled funds. Type of security: 48.5%
bonds and cash; 15.5% preferred stock; 34.2% common stock; 1.8% FHA mortgages.
Fields of investment: 37.1% governments and municipals; 13.4% utilities; 5.6% railroads;
38.5% industrials; 3.6% financial; 1.8% FHA mortgages. McHale, \textit{Common Trust Funds
Not So Common Yet}, Barron's National Business and Financial Weekly, Feb. 28, 1949,
p. 13, cols. 1-2; 88 \textit{Trusts & Estates} 156 (1949). See Stephenson, \textit{Present-Day Prac-
tices in Diversification of Trust Investments}, 24 \textit{Trust Bull.} 14, 17 (Sept. 1944) for a
discussion of the factors which limit diversification in individually invested accounts.

There are some securities, such as Canadian bonds not paying interest in American
dollars and securities of companies regularly distributing certain stock dividends, which
are appropriate for individual investment but not for a common fund. See Blakemore,
for the pro and con of mortgages as fund investments \textit{compare} Lambing, \textit{Mortgages for
Common Trust Funds}, 75 \textit{Trusts & Estates} 65 (1942), with Whittlesey, \textit{Liquidity in
Common Trust Funds}, 75 \textit{Trusts & Estates} 167 (1942).

73. Matthews, \textit{Investments for Common Trust Funds}, 83 \textit{Trusts & Estates} 81
(1946). Much more may also be achieved in selecting individual securities for their
quality (high, medium or speculative grade) and in varying the maturities of bonds to
the greatest advantage. \textit{Id.} at 82. Moreover, the ability to take security offerings in
large blocks will save the odd lot's commission and oftentimes result in a more favorable
price. Barton, \textit{Economies for the Small Trust in the Use of Common Trust Funds}, 25
\textit{Trust Bull.} 5, 12-3 (Jan. 1946); Stuebner, \textit{Investment Advantages of the Common Trust

74. Stephenson, \textit{A Decade of Common Trust Funds}, 33 \textit{Banking} 46 (Jan. 1941).
The resulting increase and stabilization of investment returns has enhanced the value of trusteeship to the income beneficiaries. And the better conservation of assets stemming from absorption by the common fund of losses which would substantially deplete the principal of an individual trust inures to the benefit of remaindermen.

To fiduciaries, the most appealing aspects of the common trust fund are the superior economies and efficiencies which it introduces into trust administration. Operational savings of from 27% to 50% have been reported wherever the plan has been tried. The primary saving, of course, derives from the efficiencies obtained by handling the investment of a number of trusts as a single unit, and possibilities of costly surcharges are reduced by the improved management techniques. In addition, the more frequent review of investments in the common fund yields useful information applicable as well to the fiduciary's non-participating trusts containing identical securities.
So far, only 57 institutions have established common funds. This may be explained in part by the conviction of pioneers in such funds that conservative unhurried, development of the new device was essential. But other factors have weighed heavily in the trustmen's mincing approach. Imperfect realization of the extent to which commingling can produce savings and accompanying profits has been a major deterrent. The necessity for procuring state enabling statutes and later amending the unduly restrictive ones to permit discretionary investment have contributed to the delay. And a widespread but false belief that the required bookkeeping is complicated has undoubtedly discouraged some trustees.

proved list and reviewing these securities monthly and, at times, even weekly. The fund is thus a valuable aid in crystallizing investment ideas and effectuating investment policies. Redman, Setting Up a Common Trust Fund, 87 Trusts & Estates 433, 436 (1948). Stuebner, supra note 73, at 26, sets out a procedure for policy formulation: weekly review of common fund holdings and transactions by (1) an investment advisory committee, (2) an executive committee, and (3) the board of directors.

81. The sixty-nine funds which they maintain total $400,000,000, McHale, supra note 72, at p. 13, col. 1, and vary in size from $464,000 to $42,000,000. 88 Trusts & Estates 156 (1949).

82. Fenninger, supra note 66, at 32.


84. See notes 58 and 59 supra.

85. See, e.g., Anderson, Practical Aspects in Common Trust Fund Creation and Administration, 27 Trust Bull. 13, 21 (Dec. 1947): “For all practical purposes we [in Ohio] are restricted to government bonds for our legal accounts, and for that reason haven't thought there was much advantage in establishing a legal fund.” This same attitude once prevailed in New York where no funds were established at all under the enabling act until discretionary funds were sanctioned seven years after the act's original passage. See Matter of Bank of New York, 189 Misc. 459, 462, 67 N.Y.S.2d 444, 447 (Surr. Ct. 1946); Maull, Answering Objections to Common Trust Fund, 79 Trusts & Estates 55 (1944).

86. Compare Clifford, Commingled Trust Funds, 11 Harv. Bus. Rev. 253 (1933) (bookkeeping unduly burdensome), with Robinson, Accounting Records for Common Trust Funds, 79 Trusts & Estates 457 (1944), who asserts that few extra forms are in fact required since an account may be opened in the trust department and a general ledger maintained the same as for any trust. Id. at 457-60.

Bogert adds the objection that the funds permit the trustee to sell to itself, thereby fostering a selfish interest opposed to the beneficiary. 3 Bogert § 677. It seems unjustified to assume, however, that any trustee would thus expose itself to a revocation of the tax advantages by so clearly violating the Federal Reserve Board's regulation. 12 Code Fed. Regs. § 206.17(a) (1938) (trustee prohibited from acquiring a non-fiduciary interest in the fund). See the Board's application of this requirement to a specific case in 12 Code Fed. Regs. § 206.101 (Supp. 1947). Bogert also criticizes the loss of individual control entailed where funds are mixed, in that the beneficiary's particular needs are likely to be neglected. But while it is true that many trusts are not appropriate for inclusion in a common trust fund, others have no unusual investment and management requirements. The common trust fund is not intended to fit the needs of every settlor and beneficiary. See Ward, The Rise of Common Trust Funds, 34 Banking 32, 83 (Nov. 1941).

The common funds do raise some questions which can be settled by proper draftsman-
While these obstructions to expanded trust service are diminishing in general importance, there are, in the case of the small corporate trustee, serious problems which must be solved before the common trust fund will be practicable. Some of the smaller corporate trustees do not have enough adaptable trusts at their disposal to set up a common trust fund of efficient size. The small institution may be further hampered by the difficulty of meeting investment prerequisites. At present the normal investments of most small companies are local securities of limited marketability which require only the Trust Officer's knowledge of local affairs. The successful common trust fund, on the other hand, requires a large proportion of readily marketable investments, which in turn demand access to statistical services and skilled personnel capable of handling periodic valuations. The result is that the common trust fund, with its considerable requirements in terms of financial and personnel resources, is beyond the means of many smaller institutions.

In the country as a whole there is a trust institution in but one county in three. The further fact that 65.52% of our 3,000 trust companies are institutions with less than one million dollars in trust assets indicates that many people have access only to small corporate trustees. Adapting commingling principles to the small institution's needs therefore seems necessary to round out the legal and practical availability of this important trust device. The areas of possible development are already clearing. For instance, small trustees might be granted permission to purchase participations in the fund of a large institution.

Footnotes:
87. It is generally agreed that there is a minimum size for efficiency but the exact amount is disputed. See, e.g., Moore, Before Starting a Common Fund, 81 TRUSTS & ESTATES 199 (1945) ($750,000); COMMON TRUST FUNDS 14 ($200,000). The smallest fund at present is $464,000. See note 82 supra and p. 937 supra.
88. Fenninger, supra note 66, at 34.
89. Ibid. Under the Board's regulations, admissions and withdrawals may only be made when the fund contains at least 40% cash and readily marketable securities. 12 Code Fed. Regs. § 206.17(c)(5) (1933). A readily marketable security is defined as one "which is the subject of frequent dealings in ready markets with such frequent quotations of price as to make (a) the price easily and definitely ascertainable and (b) the security itself easy to realize upon by sale at any time." Id. at n. 33.
90. COMMON TRUST FUNDS 15.
92. Id. at 23.
93. See Stephenson, Taking Trust Service to the People, 27 TRUST BULL. 37, 59 (Nov. 1947). In some states it might also be possible for the small trustee to purchase shares in investment trusts. See In re Rees, Ohio App., Jan. 7, 1943, 88 TRUSTS & ESTATES
owned and managed by a group of small trust companies should also be explored.\footnote{4} Possibly the management of such a fund could be delegated to a larger fiduciary on an agency basis,\footnote{5} or small institutions might obtain enough outside help by hiring investment counsel.\footnote{6} Moreover, the possibility of permitting a workable fund less complex than the present precisely regulated plan should be considered.\footnote{7}

With appropriate modifications to increase the common trust fund's utility for small institutions, this revolutionary advance in trust administration may achieve the eminence it deserves. Certainly the timorous approach adopted by most corporate trustees is no longer warranted by the facts. Failure to establish common funds where feasible not only deprives the small investor of a valuable trust service but also ignores a largely untapped source of profit to the trustee through substantial operational economies.

\textit{Investments and services.} A catalogue of the services to beneficiaries and settlors performed by the corporate fiduciary would indicate the wide range of activities which generate the out-of-pocket expenses involved in trusteeship. These include operations of a mechanical nature such as clipping bond coupons, making remittances to beneficiaries and giving vault protection to assets. Skilled activities such as investing in securities, fulfilling accounting duties and complying with taxation obligations also constitute a major portion of the typical functions. And the whole process of managing real estate and small business enterprises constitutes an important aspect of the corporate fiduciaries' investment service.

\footnote{128 (1949); Shattuck, \textit{Thorns in Trust Profession}, 88 TRUSTS \& ESTATES 84, 105-6 (1949); Stevenson, \textit{Investment Company Shares}, 85 TRUSTS \& ESTATES 141 (1947). \textit{Contra}: Marshall v. Frazier, 159 Ore. 491, 80 P.2d 42 (1938).}

\footnote{94. See Wyatt, \textit{Supervisory Policies of the Federal Reserve System}, 62 TRUST Co. 175 (1936) (suggested single common trust fund in one state); 6 P-H, \textit{TRUST Serv.} ¶ 10,061 (1948); 54 TRUST Co. 543 (1932) (address by J. W. White suggesting a single or three divisional commingled funds for investment of assets in all life insurance trusts). A variation of this approach would be establishment of bank-owned trust companies in counties or trade areas. See Stone, \textit{Fifty Years of Trust Service}, 28 TRUST BULL. 6, 9 (Sept. 1948). Trust business has already been successfully handled on a branch banking basis. REMINGTON, \textit{op. cit. supra} note 13, at 91.}

\footnote{95. See Stephenson, \textit{Taking Trust Service to the People}, 27 TRUST BULL. 37, 50 (Nov. 1947). Trust departments in twenty-seven banks affiliated with Northwest Bancorporation tried a much more extensive, though similar, scheme: the trust departments of all affiliates were to be supervised by the central organization. The plan did not prove feasible, however, probably because the members were far apart and all operating under a number of different state laws. The central organization now merely compiles figures for its 10 remaining members. See Drake, \textit{supra} note 5, at 556.}

\footnote{96. See Steber, \textit{Should Small Banks Have Trust Departments?} 88 TRUSTS \& ESTATES 98, 99 (1949) (discussing a current investigation by Pennsylvania fiduciaries into possible solutions to the small bank's problems).}

\footnote{97. See discussion of "1200 Fund," note 66 \textit{supra}. The need for amending the Board's regulation to facilitate an extension of services is being currently studied. \textit{PRESENT DAY BANKING} 199.}
The great variety of these services and their diverse presence in any particular trust pose a problem which any compensation system purporting to be based on costs must face: how to conform the fee to the expenses of trust services. In addition, any system must provide enough stability to enable trustees and settlors to foretell the cost of the service with some accuracy. While present statutes and judicial decisions achieve stability and predictability by making the fees uniform for all trusts of a given size, they neglect to conform fees to the costs of trust service. In the case of their contractual rates, some corporate trustees have already remedied this defect by constructing an equitable fee schedule based on cost analysis of typical accounts. Extension of this technique by calculating such costs for all institutions rendering service of similar quality in a given trade area, would enable computation of average costs. With proper allowance for responsibility and profit and transposition into percentage form, the averaging of costs could make possible a uniform fee schedule founded on the cost of performing ordinary services.

An alternative approach, utilized occasionally by trust companies in quoting contractual fees and extensively by other common law countries in their official schedules, is conforming the fee charged to the kind and amount of trust activity carried on in the particular case. It has been claimed that this method alone results in an equitable burden on every account regardless of size. On the other hand, the itemization of services might result in confusion and irritation to the beneficiary and, since it sacrifices stability and predictability in the interest of exact conformance to actual costs, would leave the trustee open to the charge that activity is being created.

98. See Pusey v. Clemson, 9 S. & R. 204, 209 (Pa. 1823); Comment, 42 YALE L.J. 771, 773 (1933).
99. See cases and statutes cited in note 43 supra.
100. See, e.g., Biggs, Profits—Past and Present, 84 TRUSTS & ESTATES 321 (1947); Couch, Trust Fees Based on Cost Analysis, 83 TRUSTS & ESTATES 528 (1946).
101. Recognition would thus be given to the variance among the states in the average level of such cost factors as trust size and duration and the expenses of maintaining trust departments. See 40 COLUM. L. REV. 558, 563 (1940).
102. Payne, Trust Compensation Based on Activity, 89 TRUSTS & ESTATES 139 (1945). Such charges are regularly made by banks for checking account service, 89 TRUSTS & ESTATES 461, 462 (1945), and by trust departments for corporate trust work. STEPHENSON, COMPENSATION PROVISIONS OF WILLS AND TRUST AGREEMENTS 9 (1941). Representative schedules are collected by Stephenson in STUDIES IN TRUST BUSINESS 115-7 (1st series 1938).
103. See Payne, supra note 102, at 141. “Small trust accounts are profitable if the activity is low, and large ones contrary if the activity is high. There is no rhyme or reason for one account to offset the loss on one or more other accounts.” Applying activity schedules results on the average in an increase from customary percentage fees on accounts up to $150,000, at which point the activity charge tends to decrease as compared with the percentage of income. Ibid. Compare similar statements by Lasseter, supra note 50, at 123.
104. See STEPHENSON, STUDIES IN TRUST BUSINESS 117 (1st series 1939).
Judges and legislators may not be willing to effect the wholesale departure from traditional American policy involved in switching from proportionately uniform schedules to cost-plus compensation. But they can utilize the principles involved in the latter to supplement a system of uniform fee schedules computed from ordinary costs. Many services, while not so recurrent as to warrant inclusion in averaged costs and a charge to all trusts, are so standard that a uniform fee for rendering them can be set up. Filing claims for the trust against assets of bankrupts, amending trust agreements, rendering special reports at beneficiaries' requests and supervising the repair of realty holdings are examples of special services for which an activity charge would be particularly appropriate. The adoption of such supplementary uniform schedules would add to the value of a system of uniform charges based on costs.

But these uniform schedules based on composite costs for performing the normal types of trust services would often be unsatisfactory unless accompanied by some adjusting mechanism. Many services of considerable value to the trust estate are rarely ascertainable prior to assumption of trust duties and, furthermore, defy cost standardization. Included in this class are such "unusual" or "extraordinary" services as conducting litigation, performing especially complex tax work, and participating in the reorganization of companies whose securities are part of the trust's assets.105 The growing tendency to include small business enterprises106 and extensive real estate holdings107 as legitimate provinces for fiduciary management is

105. White, New Trends in Trust Compensation, 28 TRUST BULL. 18, 21-2 (Oct. 1948) and Stephenson, Compensation for Extraordinary Trust Services, 24 TRUST BULL. 25, 31-6 (Apr. 1945), list many of the services which could be considered unusual.

106. While a business venture is not itself a proper trust investment, see 3 BOGERT § 579; 2 SCOTT 1207, trustees may, and frequently do, accept accounts which involve prolonged supervision of a settlor's business. See McHenry, Successful Operation of Business Enterprises as Executor and Trustee, 27 TRUST BULL. 30 (Oct. 1947). Indications are that trust institutions will be expected to administer such trusts to an increasing degree as they expand their activities into non-metropolitan communities. Stephenson, Taking Trust Service to the People, 27 TRUST BULL. 37, 51 (Nov. 1947). And see Foster, Property Management, 80 TRUSTS & ESTATES 285 (1945) (reporting very successful operation of farming enterprises).

Where additional compensation is allowed for managing trusts which include business enterprises, see note 108 infra, the basis for computing the fee has been the net income of the business, Note, 99 A.L.R. 961, 964 (1935). Compare McHenry, supra, at 35, unless the trustee has already been compensated in another capacity, in which case the fee from net income may be reduced. E.g., Estate of Peabody, 218 Wis. 541, 260 N.W. 444 (1935) (salary as manager); cf. Spring v. Hawkes, 351 Pa. 602, 41 A.2d 538 (1945) (salary as director and president of corporation). A different rule prevails in Australia, where gross rather than net receipts are used as the basis for the trustee's fee, with beneficiaries protected from too high remuneration by application to the court for an adjustment, see Note, 19 Aust. L. J. 143 (1945).

107. "The care and management of real estate is as much a part of trust service as is the management of stocks, bonds, and mortgages. It is a service as old, although not always as well established, as are the other types of trust service." Dyste, Real Estate
further evidence that unusual services to the trust should be treated separately.

Little has been done, however, to secure this needed flexibility except in "reasonable compensation" states where the courts profess to consider all relevant facts before making an award. In states with statutory fees for trustees the statutes seldom mention extraordinary services, and none specify the type of activity for which such compensation is to be granted. And if the statutory schedule does not provide for payment for unusual services, courts have commonly construed the omission as a denial of extra compensation. This is likewise the prevailing result where compensation agreements between the parties fail to provide for adjustments.

Some statutory amelioration of this inflexibility seems clearly necessary. But variety in fact situations renders set fee schedules impracticable. A simple provision covering the procedure for obtaining additional allowances from the courts, with the award left to the court's discretion, would be more desirable. And the court's discretionary powers should be placed at the disposal of beneficiaries as well, in order that justifiable reductions from the uniform schedules may be made in appropriate cases. Only when a uniform schedule of ordinary charges contains such elements of flexibility will it be conducive to a satisfactory relationship between trustee and beneficiary.

Management for Profit, 28 Trust Bull. 2, 3 (Nov. 1948), 87 Trusts & Estates 416 (1948). See also Ross, Real Estate as a Trust Investment, 27 Trust Bull. 30 (Nov. 1947).

Gross rather than net receipts is generally the basis for compensation for the trustee's real estate management. See 2 Scott § 242.1.


110. See 2 Scott 1388. Compare the cases cited in 4 Bogert § 976 n. 71.


112. A provision such as Michigan's would seem adequate. Mich. Acts 1939, No. 238, p. 614: "... [S]uch allowance [for extraordinary services] shall only be made upon the filing of a petition therefor, setting forth in detail such extraordinary services, or the reasons for considering the case one of unusual difficulty or responsibility, and the order making such allowance shall recite in detail the extraordinary services for which such allowance is made, giving the amount allowed for each item thereof, or the reasons for considering the case one of unusual difficulty or responsibility; and in case the order does not contain such recitals as herein required, the same shall be void and of no effect.”

113. Compare Rule 132(d) of the Delaware Court of Chancery which provides for a decrease of commissions in certain cases where the control of investments rests in someone other than the trustee or where the investment is in large blocks of securities.
Multiple trust fees. Where one or more individuals are made co-trustees with the corporate fiduciary, their contribution may reduce the corporation's costs. On the other hand, co-trusteeship may, and frequently does, increase cost by hampering efficient administration. In either case, it is pertinent to consider whether a single fee or multiple fees should be allowed and how either method can be related to actual costs.

One system for handling these co-trusteeships, which exists in several states, is to divide a single fee either equally or in proportion to services rendered. The opposite method is to allow multiple fees, with the total amount depending solely on the number of trustees. The multiple fees too may be equal or allocated in proportion to each fiduciary's services. An intermediate view more flexible than either of these is simply to award each co-trustee compensation reasonable in the light of its services. This permits an amount greater than a single fee where warranted, but prevents an unduly burdensome levy.

A further advantage of the flexible fee system, in addition to its conformance to cost, would be its tendency to promote the institution of co-trusteeship. Individual trustees are frequently appointed because the settlor feels their knowledge and training can contribute to the corporate trustee's administration of the trust. There are also instances where family reasons, such as the desire to assure that a lively personal interest will be taken in the needs of the beneficiaries, have motivated the settlor in making the designation. Today these useful objectives are difficult to attain, for

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114. Shattuck, Thorns in Trust Profession, 88 Trusts & Estates 84 (1949) suggests economic advantages where the instrument divides the duties in such a way that the corporation gets sole custody and full management power over the trust fund while the family problems are left for the individual trustee.

115. Ibid; Stayer, Should Trust Companies Encourage or Discourage Co-Trusteeships? 26 Trust Bull. 17, 18 (Sept. 1946).


118. In New York, up to three full fees are permitted where the trust exceeds $100,000. N.Y. Civil Practice Act § 1548(6); N.Y. Surrogate Court Act § 285-a(6).

119. This is the method used in New York where there are more than three co-trustees of a $100,000 trust or where co-trustees serve in a trust of less than $100,000. Ibid.


122. Joining an individual and a corporation as co-trustees was once advocated as a desirable combination of the family friend's personal judgment and direction with the corporation's experience, responsibility and equipment. Sears, op. cit. supra note 4, at 82. In spite of the waning enthusiasm of corporate trustees, many distinguished estate planners still advise co-trusteeship, frequently in the form of a committee consisting of the bank, a family advisor and a member of the family. Shattuck, Thorns in Trust Profession, 88 Trusts & Estates 84, 85 (1949).
the corporate trustee, which usually loses by the arrangement under present fee schedules, is loath to accept the duty. Individual co-trustees, on the other hand, could in many cases be persuaded to accept the trust at lesser fees than they now receive from courts and legislatures. Thus, by conforming fees to services, the corporate fiduciaries' reluctance can be overcome without an unjustified rise in the cost of co-trusteeship to settlors.

A second problem involving multiple fees arises where the corporate executor turns over assets to itself as trustee under a decedent's testamentary trust. In this situation, some of the services performed and compensated for in the executorship may effect a reduction in the cost of the trusteeship. This possibility should receive some recognition in the trust fee.

In states following the reasonable compensation doctrine, naming the same fiduciary as both executor and trustee raises no particular difficulty. The extent to which the dual capacity has affected the fiduciary's duties and responsibilities is considered in awarding a reasonable sum. Where

124. New Zealand's Public Trustee escaped most of the difficulties inherent in co-trusteeship without sacrificing its benefits by developing a system of advisory trustees. The safeguards and facilities of the Public Trustee have been preserved by not requiring joint action and responsibility and, at the same time, both the Trustee and the beneficiaries have secured the benefit of expert and trusted advice on discretionary matters. See Baird, Advisory Trustees, 87 Trusts & Estates 167, 168 (1948). Corporate trustees might well profit from more extensive use of such an arrangement, particularly where they accept the supervision of a business enterprise. See note 106 supra.
125. Executor's fees are generally regulated in the same manner as trustee's fees: they may be allowed by the court in its absolute or limited discretion or they may be fixed by statute. See Comment, 42 Yale L. J. 771 (1933). Where statutory schedules are prescribed, the fee is usually based on the value of the property handled by the executor rather than on the income received during his administration. See Shelton, Comparative Fees of Executors, 81 Trusts & Estates 491 (1945).
126. See Report of Committee on Costs and Charges, Trust Section, North Carolina Bankers Association, 8 P-H Trust Serv. ¶14,746 (1948), which recommends that the executor-trustee's annual principal commission as trustee should not begin until after the first ten years of the trust in recognition of services to principal performed and compensated for as executor.

Pennsylvania had the only statutory prohibition against awarding more than one principal commission to an executor-trustee. Pa. Laws 1864, no. 52, as recodified, Pa. Stat. Ann., tit. 20, §813 (Purdon, 1938). The repeal of this prohibition in 1945 was inconclusive, Pa. Laws 1945, no. 90, and left the present status of executor-trustee commissions in some doubt. The leading case thus far rejected any implication that Pennsylvania fiduciaries are now entitled to additional compensation as a matter of right and declined a requested allowance on the ground that the trustee had already been adequately compensated as executor for such services as she had rendered in her dual capacity. Snow's Estate, 58 D. & C. 485 (Pa. 1947). A corporate trustee has now prepared a case which will be carried through to the Pennsylvania Supreme Court.
fees are fixed by statute, however, they may be interpreted as requiring
double commissions for handling the same property without regard to the
measure of service performed. But the more desirable analysis denies the
second statutory compensation on the principal unless the two functions
are clearly differentiated. This is, in effect, a requirement that the exec-
utor-trustee actually earn the compensation which it seeks. As such, this
rule may be readily adapted to the overall objective of conforming fees to
costs.

Some deviation from uniform schedules set up to cover the single fee
situation will usually be required where the contributions of co-trustees and
executor-trustees are thus measured. This necessity for an increase or
decrease from the standard allowance need not, however, eliminate the
predictability of the uniform fee system. The compensation of the sole
trustee would remain as a standard of measurement, and deviations from
this standard to allow payments to co-trustees and executor-trustees would
themselves become increasingly predictable as the system continued in
operation.

Operating risk losses. Every business venture must face the possibility
that in the course of its operations it may make mistakes which will add to
its costs. The fiduciary, however, faces an additional hazard growing out
of its responsibility for the funds entrusted to its control: if the trustee

in an effort to establish a rule which will permit the additional fee as a general practice.
Communication to the YALE LAW JOURNAL from George C. Robinson, Trust Operations
Officer, Fidelity-Philadelphia Trust Co., Jan. 25, 1949. Voluminous testimony has been
taken in the trial court for the purpose of establishing a factual basis to the increased
costs and decreased income, which corporate fiduciaries claim is characteristic of their
personal trust business. See Record of Testimony, Estate of Ella Williamson, Orphan's
Court of Philadelphia County, December 8, 1947. The trustee in this case is also attack-
ing the Pennsylvania rule as to the time for taking the principal commission. See note
162 infra.

128. See Note, Double Compensation for Testamentary Fiduciary Acting as Both
Executor and Trustee, 44 YALE L.J. 523, 526 (1935); 4 Boger § 978; 2 Scott § 242.9.
The double commission problem may also arise in other dual-fiduciary situations. E.g.,
Rose v. Bank of Wadesboro, 217 N.C. 600, 9 S.E.2d 2 (1940) (administrator-guardian
granted two commissions); see Patterson v. Old Dom. Trust Co., 149 Va. 597, 615, 140
S.E. 810, 815 (1927) (trustee-special commissioner denied two commissions).

129. For a clear analysis, see Bemmerly v. Woodard, 136 Cal. 326, 68 Pac. 1017 (1902).
New York accepts as the criterion of separation whether the will clearly distinguishes
between the two functions. Compare Matter of Schlieman, 259 N.Y. 497, 182 N.E. 153
(1932) (double compensation granted) with Matter of Ziegler, 218 N.Y. 544, 113 N.E.
553 (1916) (double compensation denied). See the cases collected in Note, 84 A.L.R. 667
(1932).

In the few states in which executorships and testamentary trusteeships are admin-
istered under the supervision of separate courts, (e.g., Del. Rev. Code c. 98 (1935),
executorships-Register of Wills; id. at § 4400, trusteeships-Court of Chancery), the pro-
cedural separation appears to be along functional lines. The fact that the testamentary
trustee previously served as executor does not then affect the compensation allowed in the
trusteeship. Communication to the YALE LAW JOURNAL from James W. Allison, Vice
President, Equitable Trust Co., Wilmington, Delaware, January 19, 1949.
fails to perform the duties imposed under the trust as would a man of ordinary prudence in like circumstances, he will be liable to respond in damages for any loss.\(^{130}\) Where bonds as security against these losses are required of corporate fiduciaries,\(^{131}\) their cost is passed on to the trust estate.\(^{132}\) And where the fiduciary acts as a self-insurer, in effect pledging its assets as security for the prudent performance of trust duties, the establishment of reserves to absorb compromise settlements and surcharges is a recognized cost factor in trustees' compensation.\(^{133}\)

Scientific prediction of losses is hampered by at least two uncertainties. First, the probability of negligence will vary with the skill and internal organization of each fiduciary.\(^{134}\) Second, the extent to which depression stimuli will induce beneficiaries to seek surcharges is equally uncertain.\(^{135}\) But the problem does not appear insuperable, for surety companies have dealt with it successfully in valuing their services to trustees.\(^{136}\) A substantially equitable calculation might even be made by simply utilizing the average annual loss figure for a representative past period.\(^{137}\)

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130. 3 BOGERT c. 32; Continental Ill. Nat. Bank & Trust Co. v. Kelley, 333 Ill. App. 119, 76 N.E.2d 820 (1948) (forfeiture of compensation due to self-dealing). It can be argued that the corporate trustee should be held to a greater degree of care than the individual nonprofessional trustee since it holds itself out as a specialist in the field. 2 Scott § 174.1. But see Moore, supra note 28, at 653.


134. See MacLennan, Trust Cost Accounting, 86 Trusts & Estates 409, 413 (1948).

135. See Moore, supra note 28, at 647.

136. Callahan, supra note 132, at 30, suggests a comparison with the surety as a means of calculating the responsibility factor.

137. ROBINSON, Cost Accounting for Banks and Trust Companies 57 (1947) (cited hereafter as ROBINSON, Cost Accounting).

When calculating the appropriate charge, some weight should probably be given to the selectivity with which trustees undertake their obligations and to the elaborate system of internal safeguards employed to control decisions, see Stephenson, The American System of Trust Business c.8 (1936), coupled with government supervision to ensure that these safeguards are utilized. See, generally, 4 BOGERT § 920; NEILAN, Trust Examination passim (1939). Some recognition of these factors of care and responsibility has already been given by legislatures in abandoning bond requirements for corporate fiduciaries, see e.g., Tex. Stat. Ann., arts. 4982, 4983 (Vernon, 1940), and by surety companies in quoting rates to them a third-lower than to individual trustees. 25 Trust Bull. 2 (Dec. 1945). Settlors also take the corporate trustees' greater financial responsibility
Summary

Conforming fees to services, if coupled with efficient operational techniques, will put trust departments on an independent paying basis. Subsidization of the department or of particular fiduciary activities will then be unnecessary. As changes in the general level of costs take place, the same techniques of cost analysis which are essential to instituting uniform schedules can be utilized, with relatively little time lag, to adjust rates to the new conditions.

Putting theory to work

Discovering the facts. Before any system of trustee compensation can be devised, it is necessary to know more about the trust business than can be gleaned from statute and decision. One of the major difficulties encountered in any objective appraisal of the corporate fiduciary’s compensation is the lack of official sources of information. Significant trust statistics are almost non-existent and impartial investigations by governmental authorities have been conducted only in New York.

Responsibility for the lack of statistics and informative studies must rest largely on those state legislatures and banking departments which have failed to realize the necessity for an informed attitude toward a business which controls, in personal trust accounts alone, 36 billion dollars of liquid assets. Many influential trustmen would apparently welcome the interest into consideration by contractually relieving them from the bond requirement. See note 132 supra.

138. The Comptroller of the Currency is the only federal agency at present publishing trust statistics as part of its annual report. The information contained is limited in scope and confined to the fiduciary activities of national banks without any breakdown along regional or state lines. ANNUAL REPORT OF COMPTROLLER OF CURRENCY 177–8 (1948). At least five state banking departments (Massachusetts, Connecticut, California, Illinois, Pennsylvania) publish statistics, but these vary in scope and utility. See Stephenson, Statistics of Trust Business, 27 TRUST BULL. 14, 23–4 (May 1948).

All trust statistics, official and unofficial, suffer from the present lack of any system approaching uniform valuation of the trust funds. The four methods generally employed—cost-or-inventory, par-or-face, unit control, and assessed value—lead to widely varying results and bear no relationship to current market values. Id. at 15. But see Zara, The Statistical Tower of Babel, 64 TRUST Co. 407, 410 (1937).

Periodic revaluation to market value seems a better basis for statistics than any of the foregoing systems, because it is meaningful in terms of the quality of securities held, and is, in effect, so recognized and endorsed by federal regulation. National banks are required to determine the current value of their investment at least once every twelve months. 12 Code Fed. Regs. § 206.6(c) (1938). And the Federal Reserve Board’s regulation on common trust funds requires a valuation at quarterly periods. 12 Code Fed. Regs., § 206.17(c) (4) (Supp. 1945). Moreover, pay-as-you-go schedules may make the current value of principal an important consideration. See p. 953 supra. The problems involved in persuading trust companies to adopt this method in pursuance of the goal of more adequate statistics are discussed and evaluated by Stephenson, supra at 16–22.

139. See note 34 supra.

140. See note 5 supra.
of officials in the collection of trust facts. And such a development appears essential before any significant progress can be made in conforming trust fees to services performed.

Essentiality of cost accounting and cost analysis. The amazing neglect of cost accounting in trust work is, like the paucity of official statistics, a barrier to any compensation reform. It is, moreover, an obstacle of particular concern when an attempt is made at conforming the fee system to costs.

The failure to use cost accounting procedure can hardly be explained on the basis of institutional size, since both large and small trust companies have overlooked its possibilities. This neglect may be due to a lingering attitude on the part of bank directors that trust business is a side-line activity, with its losses properly underwritten by the bank as a whole. Or it may derive from the mistaken belief that there are innate complexities and expenses incident to establishing and conducting effective cost accounting.


142. The Chairman of the Committee on Costs and Charges, Trust Division, A.B.A., has summarized the current status of cost accounting as follows: “In spite of the fact that this committee has continued ever since [1929] to preach the gospel of determining trust costs to trust institutions from coast to coast and regardless of similar endeavors by committees formed by state and local fiduciary associations, the progress to date has been most disappointing.” Wilson, Some Suggestions for Taking the Guess Work Out of Trust Profits, 28 Trust Bull. 4 (Oct. 1948). Pennsylvania has led all other states in the development of trust cost accounting, yet only one out of every four departments has a cost accounting system. 88 Trusts & Estates 43 (1949).

Banking as a whole suffers from a like neglect. See Robinson, Cost Accounting 58: “For some unknown reason cost accounting has not as a general rule, been looked upon with favor by bankers. A hostile attitude on the part of bank management has retarded the development of cost accounting.”

143. Wilson, supra note 142, at 5; 88 Trusts & Estates 43 (1949) (reporting $100,-000,000 departments without any apparent interest in knowing their profit or loss).

144. If a trust department is in fact losing money, this attitude may be prejudicial to the interests of stockholders who have invested funds in the bank as a whole with some expectation of gain from trust activities and to bank customers who pay for the burden of trust work in increased fees for services rendered by the saving and commercial departments. See Wilson, supra note 142, at 6-7. A steadily losing department may also manifest its ills in the form of lower quality service. Ibid. Schwalm, Trust Service at a Profit, 84 Trusts & Estates 631, 632 (1947).

145. Cf. Lasseter, Taking Guesswork Out of Trust Costs, 85 Trusts & Estates 57, 124 (1947): “There is no trust department too small for a cost study and it is inconceivable that a bank or trust company qualified to render fiduciary services does not have among its trust or auditing personnel someone who could do a thoroughly creditable job of a study.” See pp. 950-1 supra.

146. See Robinson, Cost Accounting 58: “Cost accounting expense can be controlled just as any other expenses. Any figure set by management within reason will be sufficient. Several of the largest banks in the country employ only two clerks on cost accounting procedure and achieve substantially accurate results. One large bank operates with only one clerk.”
Whatever may be the reasons for its neglect, cost accounting is clearly needed in trust work. As in other businesses, it can make possible both better service and lower expenses. Particularly in the case of the corporate trustee, the intangible cost factors demand scientific control. Furthermore, at a time when corporate fiduciaries are seeking greater compensation, and need some equitable basis to attain it, the first step must be cost accounting.

The further step of the cost analysis of individual accounts based on a previous practice of cost accounting contains the key to advance in the principles of trust compensation. Extrastatutory arrangements among the parties become practicable only when specific costs are transposed into a fee schedule uniformly and impartially applied. And courts and legislatures would hardly be justified in abandoning customary yardsticks for new fee schedules until the basis is laid by thorough investigation of fiduciary costs.

Specifically, what is needed is knowledge of the trustee's profit and loss (1) from total trust operations, (2) from each class of service such as testamentary trusts and executorships and (3) from each individual account carried by the company. The basic approach is essentially a refinement of the income and expense accounts already maintained by all trust in-

147. Id. at 1-2. Corporate fiduciaries have been frequently scored for their failure to use modern operational methods and to revise now antiquated practices for the review and management of securities. See, e.g., Shelor, Trust Business Can Be Profitable, 80 Trusts & Estates 41, 42-4 (1945) (setting forth a number of steps to better management, including cost accounting).

148. "The possibilities for controlling expenses by means of cost accounting figures are practically innumerable and will depend largely upon the size of the organization and the initiative of the cost accountant." ROBINSON, COST ACCOUNTING 3. See, also, the same author's Trust Department Expense Control, 86 Trusts & Estates 109 (1948) (significance of the combination of cost accounting, activity control, budgets and strong management).

149. In contrast with industrial enterprises, the tangible cost factors involved in rendering services are confined to such minor items as stationery. Salaries account for the major expense, see Hoyle, New Trust Cost Analysis, 87 Trusts & Estates 171, 172-3 (1948) (46 trust departments: salaries over 70%; occupancy of quarters nearly 9%), and, unlike industrial costs, cannot be individually applied to the product. ROBINSON, COST ACCOUNTING 7. It is thus obvious that some method for ascertaining and controlling personnel and other overhead costs is essential if expenses are to be lowered. They must be lowered, many trustmen believe, if profits are to be increased, since fees are about as high as the market will bear. See, e.g., Phelan, Post-War Market for Trust Service, 80 Trusts & Estates 31 (1945). But Alton, Adequate Compensation for Trustees, 27 Trusts Bull. 5, 6 (Dec. 1937), expresses doubt as to the likelihood of costs being controlled because of free services to the government such as tax collection.

150. See ROBINSON, COST ACCOUNTING 4-5. Renegotiation of the compensation for outstanding trusts has been particularly effective where a standard cost basis has been employed. See, e.g., 87 Trusts & Estates 472, 473 (1948) (Old Colony Trust Co. of Boston has renegotiated 2534 accounts—80% of its personal trusts).

151. Lasseter, supra note 145, at 57.
One of the principal procedures used is to classify total expenses according to type (salaries, rent, insurance, etc.), thus enabling expenses to be allocated to major work units (testamentary trust, guardianship, etc.), and a unit cost determined for each type of service performed. Application of unit costs to the activity of each trust account then yields a cost figure for the trust from which net profit or loss may be readily calculated. Infinite variation in detail and procedure may be devised by competent accountants facing particular sets of institutional problems.

Corporate trustees which institute an adequate cost accounting system and cost-analyze their individual accounts will then be in a position to exert scientific control over expenses and factually justify requests for increased compensation. However, in order to achieve the maximum benefits from the potentials inherent in cost accounting, a uniform procedure should be adopted by all the trust companies in a particular trade area. It would then be possible to compare costs for the purpose of developing more efficient operational methods. A pool of cost figures would not only provide the facts prerequisite to convincing courts and legislatures that the present inadequate fee system should be replaced, but would also constitute the information required to effectuate a system of compensation based on costs.

**Who Should Pay and When**

Percentages representing costs do not alone make a fee schedule. In order to yield a dollars and cents compensation, these percentages must be applied either against income, to the detriment of the income beneficiary, or against principal which otherwise would go to the remainderman. At present the fee comes largely from annual income payments, but usually there is also a commission based on a fixed percentage of the principal.

Where a principal commission is allowed, the trustee and the income beneficiary are both concerned with the time of its payment. From the trustee’s viewpoint, a 2% principal commission on a twenty-year trust taken at inception is worth twice as much as the same commission at termination.

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154. A table of major and minor classifications with the basis for their allocation to departments, divisions and expense units has been compiled by Robinson, Cost Accounting c. 4.
155. See id. at 9-10 for a graphic presentation of the whole procedure in the form of an expense flow chart.
156. Id. at 49; Lasseter, supra note 145, at 57. For suggested accounting methods designed particularly to meet the needs of small institutions, see Laffoley, Machine Accounting for Smaller Trusts Departments, 88 Trusts & Estates 111 (1949); Weig, A Cost System for a Personal Trust Account in a Small Trust Department, 22 Trust Bull. 7 (July-Aug. 1943).
158. See, generally, Robinson, Cost Accounting c. 15.
tion. The income beneficiary, on the other hand, loses by a payment at the beginning, for he then will receive the income on only 98% of the original investment. Apart from these considerations, payment of principal commission in a lump sum seems markedly less fair than annual payments. The amount of the lump sum is inherently fortuitous, in that it depends on the state of the economic cycle in the year of payment. When the principal commission is paid annually, the total fee eventually received fairly represents the value of the assets over the life of the trust.

The importance of considering who should pay the trustee and when the compensation should be taken was not reflected in standard practices until recently. At the time that these practices were solidifying into statute and court rule, realty was the predominant corpus of nearly all trusts. The impracticability of collecting an annual fee from principal gave rise to the procedure of delaying such compensation until termination of the trust, when the property would be distributed in liquid form. Although trusts are now composed largely of readily marketable property, the old practice is to a considerable extent still followed.

Lump sum payment of the principal commission, with annual compensation confined to income, proved satisfactory as long as the prime objective of trusteeship was conserving the trust res. But when trustees became active managers with the duty to make the property productive for life beneficiaries, both the beneficiary and the trustee got caught in the squeeze between higher costs and a lower return on trust investments. At the same time, settlors began to extend their trusts to the maximum duration permitted by law in order to effectuate tax savings. But the principal commission remained the same regardless of the trust’s duration.

159. E.g., 2% of the principal at inception, if compounded annually at 4%, would be
worth 4.38% of the same sum at termination. Stephenson, Studies in Trust Business
108 (1st series 1938).

1946).

161. See note 26 supra.

162. See note 26 supra.

Pennsylvania is one of the major jurisdictions in which the trustee is compelled to wait until termination. See Wilson, Extraordinary and Interim Trust Fees, 84 Trusts
& Estates 627, 629 (1947). The general rule has been recently stated in Powers’ Estate,
58 D. & C. 379, 381-2 (Pa. 1947): “... [A] trustee is not entitled to a commission on
the principal of an estate until the trust expires, or the particular trustee’s relation to it
ends ... unless there are circumstances of an unusual and extraordinary character,
and the trustee has increased the estate by great care and skill.” See note 127 supra.

163. See note 26 supra.


165. Where the term is short, the lump sum award of an unvarying principal commission may, of course, be unfair to the beneficiaries. If the trust is of long duration, the trustee may find it inequitable. In many circumstances, an individual trustee will find it more so than a corporate trustee. For instance, individual trustees who die prior to termination of the trust not only are denied the fruits of their labors in their lifetime, but
The desire to remedy this inadequacy, as well as to apportion the burden of current expense between income beneficiaries and remaindermen, has led to introduction of the pay-as-you-go concept, a distribution of the annual commission between both principal and income. Under such a plan, remaindermen receive less principal than heretofore, the difference usually being distributed between a greater return for income beneficiaries and an increased total commission for the trustee. Equally important to the trustee, pay-as-you-go plans spread his earnings throughout the life of the trust.

their heirs are penalized by reductions through inheritance, estate and income taxes levied at high brackets due to the addition of the full sum to the estate in a single year. Where the trust terminates during the individual trustee's lifetime, the lump sum payment will again push the taxpayer into a higher income tax bracket. And the individual trustee can seldom, if ever, benefit from a tax adjustment under the lump sum provisions of the Internal Revenue Code; for such adjustment to be made the Code requires the receipt of 80% of the total commission in a lump sum, Int. Rev. Code § 107(a), and the annual income commission would almost invariably be more than 20% of the total. For a fuller statement of the individual trustee's position, see Brief of T. Williams Roberts, an Individual Trustee, as Amicus Curiae, Estate of Ella Williamson, Orphans' Court of Philadelphia County, Dec. 8, 1947. The compensation reforms advocated in this comment are thus of concern to the individual as well as the corporate trustee.

166. This ideal of charging to each income beneficiary and remainderman the costs incurred in advancing his interest is not a goal of all pay-as-you-go plans. Thus, while most present plans provide for an annual charge on income and one on principal, in some localities, notably in western states, the entire fee is based on principal alone. White, New Trends in Trust Compensation, 28 Trust Bull. 13, 16 (Oct. 1948). Moreover, it is possible to measure the rate against both principal and income and yet actually take the fee exclusively from one or the other source. See Stevenson, Studies in Trust Business 107-8 (1st series 1938); Delaware Chancery Court, Rule 132(g) (charitable and other perpetual trusts).


White, New Trends in Trust Compensation, 28 Trust Bull. 13, 25-9 (Oct. 1948), reproduces in comparative form the contractual pay-as-you-go schedules presently utilized by the fiduciaries in 29 cities throughout the country who are operating under such plans.

The chief drawback to pay-as-you-go plans under current practices is the lack of any uniform method of valuation. This is particularly disadvantageous in view of the fact that the annual commission is generally retained without filing an annual account. But a solution to the valuation problem does appear to be evolving. See note 138 supra. Compare the New York statute which makes original value presumptive of the current value with the option open to revalue on another basis. N.Y. Civil Practice Act § 1548(3), N.Y. Surrogate Court Act § 285-a(3).

rather than concentrating them at termination; and where each annual payment is based on the value of the corpus at that time, compensation tends to vary with the business cycle.

Pay-as-you-go plans do not, however, provide a complete answer to the problem of the effect of cyclical fluctuations, for changes in valuation of the corpus may not accurately reflect changes in trustees' costs. Moreover, it is too impractical to adjust uniform schedules to costs at every fluctuation of the economy. The only complete cure would be to abandon entirely the income-principal basis for compensation in favor of an ad hoc cost-plus policy. And it is at least debatable whether such a policy might not dampen the trustee's incentive to render efficient service of good quality—an incentive retained where the exigencies of the market are allowed some play in determining the amount of compensation. It would seem, therefore, that adjustment of the uniform schedules to account for long range rises and falls in the general level of costs would be sufficient to keep the fees on an equitable basis.

**Conclusion**

In the last half century, the corporate trustee, a minor offspring of the insurance business, has come into its majority. Whether it has also attained social maturity depends on its ability to meet the needs of the small investor. Indeed the whole future pattern of institutionalized trusteeship will be affected by the solution to the vexing problem of how to render quality service at a reasonable price. Improved operational techniques such as cost analysis and the common trust fund, coupled with a revised compensation system which conforms to costs, appear to be the answer. But if there is some unlikely incompatibility of profit with trusteeship which prevents reform from resulting in needed trust facilities, a non-profit public trustee may well be the only resort for the small investor.

At any rate, the corporate trustee should no longer be required to seek out the answer on its own. Customary fees applicable to the individual fiduciary have congealed into the law governing the institutionalized trustee due to the acceptance of that custom by court and legislature. Any effective change must come from them. If state supervisory authorities realize this, they have not manifested their realization in any integrated form. The essential task of giving effect to the public's interest in the broad field of fiduciary reform still awaits their attention.

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169. But see Bardt, *Flexible Compensation*, 88 Trusts & Estates 80, 82 (1949) who advocates a year-to-year revision on the basis of then prevailing costs.
170. See note 102 supra and p. 941 supra.