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TRUSTS-NATURE OF MASSACHUSETTS OR BUSINESS TRUST

TRUSTS—NATURE OF MASSACHUSETTS OR BUSINESS TRUST.—The exact nature and legal incidents of the business trust, better known as the Massachusetts trust, have been put in question several times in recent years. There have been many conflicting decisions, and they represent varying degrees of hostility or favor towards a method of doing business which seems to possess many of the advantages of incorporation without carrying its burdens. It has recently been said: "The different and confusing conceptions of the law upon the subject of the Massachusetts trust, as evidenced by the many decisions of courts of the different states, and in discussions by the text-writers throughout the country, is our apology for this extended discussion." *Continental Supply Co. v. Adams* (Tex. Civ. App. 1925) 272 S. W. 325.

As the name would imply, this method of doing business is most common in Massachusetts, and is simply a development of the common law trust. It rests on an agreement, or declaration of trust, between two sets of parties, one of which (cestuis que trustent) usually transfers property to the other (trustees) in consideration of the agreement by the latter to hold the legal title to and manage the property according to the terms of the agreement, the profits going to the cestuis. The interest of the cestuis is divided into transferable shares, similar to shares of stock in a corporation, and these shares are customarily represented by certificates. The trustees may have varying degrees of control, from absolute power over the property, with power to elect their successors, to a mere managerial function, where they are subject to the

will of the cestuis from time to time. It is customary for the liability of the cestuis to be limited in the agreement to the property actually invested, and to attempt to limit the liability of the trustees by providing that in all contracts there shall be a stipulation that the third party will look only to the trust estate for damages or enforcement. Thus it will be seen that the object of the business trust is to secure the limited liability and comparatively indefinite succession of the corporation, with none of the correlative red-tape, special taxation and statutory directors' liability.

A recent Michigan case has involved the status of such an organization. *Forgan v. Mackie,* 232 Mich. 476, 205 N. W. 600. The declaration of trust in that case was made in Massachusetts, between nine trustees and a Delaware corporation, by the terms of which the latter corporation transferred certain assets to the trustees in return for which it was given certificates representing preferred and common shares of beneficial interest in the trust. The trustees were authorized to issue and sell other shares, though it does not appear that they did so. The corporation therefore was the sole beneficiary. As such, its rights were merely to receive the profits and to share in the distribution of the assets upon the termination of the trust. It was provided that the trustees in their discretion could call meetings of the shareholders, but the only purpose of these was to advise the trustees. No control of any sort could the shareholders exercise. The trustees were, so far as practicable, to do business under, and be designated by, the name of "The Commercial Acceptance Trust". It was held that such an organization was, for the purpose of suit, a legal entity; that it, and not the trustees, owned a note endorsed to "The Commercial Acceptance Trust"; and that suit must be brought in the trust name, and not in the name of the trustees.

Forms of doing business similar to the Massachusetts trust have been variously characterized as partnerships (*Frost v. Thompson,* 219 Mass. 360, 106 N. E. 1009; *Wells v. Mackay Telegraph Cable Co.* (Tex. Civ. App. 1921) 239 S. W. 1001), joint stock companies (*Spotswood v. Morris,* 12 Ida. 360, 85 Pac. 1094; *Clagett v. Kilbourne,* 1 Black 346, 17 L. Ed. 213) and pure trusts (*Williams v. Milton,* 215 Mass. 1, 102 N. E. 355; *Betts v. Hackathorn,* 159 Ark. 621, 252 S. W. 602). The reasons for these distinctions rest largely upon the particular trust agreement under which the organization operates, upon the powers which it grants and the obligations it imposes. Thus in Massachusetts the usual division is between true trusteeships and partnerships. Where the complete control is in the trustees, it is held to be a trust. *Mayo v. Moritz,* 151 Mass. 481, 24 N. E. 1083; *Williams v. Milton, supra.* But if the shareholders have substantial control, as removal and election of the trustees, or power to change the declaration of trust, it is held that the organization is merely a partnership or association between the shareholders. *Frost v. Thompson, supra; Hoadley v. County Comm'rs of Essex,* 105 Mass. 519. The United States Supreme Court, on the other hand, has distinguished between various forms of the business trust on other grounds. In *Eliot v. Freeman,* 220 U. S. 178, 31 Sup. Ct. 360, it was held that a pure trust was not within the purview of a statute taxing "every corporation, joint stock company or association organized under the laws of the United States, or of any state" because a trust existed under the common law, and not by virtue of any statutory law. In *Crocker v.*

Malley, 249 U. S. 223, 39 Sup. Ct. 270, it was held that a tax on income accruing to "every corporation, joint stock company or association organized in the United States, no matter how created or organized" did not apply to a pure investment trust, for it was not within the usual meaning of a joint stock company, and there was no association. However, this decision was narrowed somewhat in a later case, *Hecht v. Malley*, 265 U. S. 144, 44 Sup. Ct. 462. This involved an excise tax on corporations, joint stock companies and associations organized in the United States, no matter how created or organized, which were doing business. The court held the tax applicable to business trusts, and explained the *Crocker* case on the ground that that was an income tax, that there were separate sections in that act for trustees, and that to include the business trust within the terms "corporations, joint stock companies and associations" would result in double taxation. Since the tax in the *Hecht* case was one on the privilege of doing business, the court found nothing to indicate an intention of congress to exclude the business trust from its operation. This court, then, seems to differentiate trusts on whether they are for purposes of investment or for carrying on business.

There have been a great number of decisions in Texas involving Massachusetts trusts and there is a decided conflict among the several courts of civil appeals of that state as to the standing of the business trust. In *Wells v. Mackay Telegraph Cable Co. supra*, the court said that the only way of limiting liability of persons doing business in that state was under the corporation and limited partnership statutes, and, therefore, that business trusts were to be considered nothing more than general partnerships. In another case the Massachusetts rule of distinction was recognized as valid in Texas, though the organization there considered was held to be a partnership. *Morehead v. Greenville Exchange National Bank*, (Tex. Civ. App. 1922) 243 S. W. 546. In still another case, involving a pure trust, the court said: "We do not think there is anything in the articles of our statutes or in the rule of procedure that limits or restricts the right in respect to the creation of trust estates long recognized by equity and the common law, but that such trust and the right of trustees to act for associations of persons has been expressly recognized by the Legislature of Texas since the trading or business trust became a common institution in this state. No feature of the common law of England is more thoroughly established or more generally recognized than the subject of trust estates and the right to its creation, and never limited by our Constitution or laws." *Cattle Raisers' Loan Co. v. Sutton*, (Tex. Civ. App. 1925) 271 S. W. 233. In this last case the court held a beneficiary under the trust not liable for trust debts. Few of these cases have been carried to the supreme court of the state, the only ones found being *Thompson v. Schmitt*, (Tex. 1925) 274 S. W. 554, and two others decided at the same time involving the same point. In these cases it was held the organizations before the court were merely partnerships because the trustees were agents of the other interested parties. In answer to questions put by the court of civil appeals in the *Thompson* case in regard to the standing of the business trust in Texas, the court was not very clear, but seemed to indicate that no such method would be allowed, for the reasons stated in *Wells v. Mackay Telegraph Cable Co. supra*. The cases *contra*, however, from the courts of civil appeals, were not noticed.

The Michigan case of *Forgan v. Mackie* is somewhat similar to a very recent Massachusetts case, *Bouchard v. First People's Trust,* 148 N. E. 895. In this latter case suit was brought against a Massachusetts trust in the trust name, under a statute allowing associations to sue and be sued in the name of the association. "Association" was defined by statute as a "voluntary association under a written instrument or declaration of trust, the beneficial interest of which is divided into transferable certificates of participation or shares." Mass. Gen. Laws 1921, ch. 182. The court held that since the declaration of trust allowed no control over the trustees at all, and did not provide for shareholders' meetings, there was no association, and hence the suit should have been brought against the trustees individually and not against the trust.

The court in *Forgan v. Mackie* treated the trust as an entity—as having an existence separate and apart from the trustees. It regarded the trust, and not the trustees, as the owner of the note. "The chose in action upon which this case is founded was owned by The Commercial Acceptance Trust." "No endorsement of the note or assignment of the contract to them individually or collectively by the Commercial Acceptance Trust is shown." This is hardly in accordance with the usual conception of a trust, or with the declaration of trust here involved. The trustees are generally considered the owners, even though for convenience they transact business under an assumed name. *Hull v. Newhall,* 244 Mass. 207, 138 N. E. 249.

It would appear from the decision in the *Forgan* case that the court is inclined to treat this as a legal entity because, under any other holding, it sees a way for foreign corporations to do business within the state without complying with the laws relating to foreign corporations, for a Delaware corporation was sole beneficiary under this agreement. However, this would seem a problem for the legislature, rather than the court, to work out. The court supports its conclusion by reference to the Foreign Corporations Law, in which "corporations" as used therein is defined to be any association or joint stock company having any of the privileges *of corporations* not possessed by partnerships or individuals. Comp. Laws Mich. (1915) sec. 9071. The court then proceeds to find powers and privileges in the trustees and beneficiaries which are not possessed by individuals or partnerships, and finds the trust to be a corporation under that law. This finding, however, is subject to the criticism that this trust is not an association or joint stock company (see *Bouchard v. First People's Trust, supra,* and *Crocker v. Malley, supra*) and that the powers and privileges mentioned are not peculiarly those of corporations. An Idaho statute, in the same terms as the Michigan statute in question, was interpreted as not applicable to joint stock companies formed under the common law. *Spotswood v. Morris,* 12 Ida. 360, 85 Pac. 1094. The court there said: "The association under consideration is not a corporation exercising any of the powers or privileges of corporations not possessed by individuals or partnerships. It is a voluntary association. *To possess or exercise powers or privileges of corporations requires a sovereign grant*—and franchises which said association has not and does not profess to possess. There are, however, associations and joint stock companies that have and exercise under grant of the sovereign, powers and privileges of corporations not possessed by individuals or partnerships, to which the language of the statute is applicable." A Kansas case, decided after the

above case, in construing a statute somewhat similar to the Michigan statute, but which omitted the words "of corporations", held Massachusetts trusts to be corporations under the statute, but expressly recognized the distinction between that statute and the Idaho and Michigan statutes. *Harris v. United State and Mexico Oil Co.* 110 Kans. 532, 204 Pac. 754. The court indicates that were the words "of corporations" present, they would hold with the Idaho court. See also, *People v. Coleman*, 5 N. Y. S. 394; BIENNIAL REPORT OF THE ATTORNEY GENERAL OF MICHIGAN, 1923-1924, pp. 93, 355.

An interesting question for the court to solve would be presented if the trustees had adopted no assumed name, as they certainly could have done business without it.

A further point is raised by counsel for the trust in his brief, though not discussed by the court, namely, that this decision deprives the trustees of their property without due process of law, contrary to the Fourteenth Amendment, when it holds the trustees do not own the property. The writer understands that this case will be appealed to the United States Supreme Court on this ground, and the outcome will at least be interesting. L. B. P.