Michigan Law Review

Volume 45 | Issue 5

1947

TRUSTS-CREDITORS' CLAIMS AGAINST THE TRUST PROPERTY-LIABILITY OF TRUSTEES IN REPRESENTATIVE CAPACITY

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TRUSTS—CREDITORS' CLAIMS AGAINST THE TRUST PROPERTY—LIABILITY OF TRUSTEES IN REPRESENTATIVE CAPACITY—Suit upon two notes signed by appellees, "Trustees, trading as the Annie Reisch Investment Company, a Common Law Trust of Sangamon County, Illinois." The notes, due

in four months after date of execution, were purchased by the plaintiff, appellant, from the payee bank's receiver nine years after their maturity. This action was begun by complaint and cognovit and judgment was entered against the makers individually and as trustees. The individual defendants filed motions to open judgment against them individually; and upon motion for a summary judgment filed by defendants, *held*, by section 20 of the Negotiable Instruments Law,[1] defendant trustees are exempted from personal liability, trustees being protected by the statutory words "or in a representative capacity." While there was no express authorization in the trust instrument for the defendants to execute judgment notes, yet the provisions of the instrument were broad enough to authorize such, so that section 20 of the N.I.L. was applicable. A trust estate can be held liable at law for its authorized contracts.[2] *Smith v. Reisch*, 329 Ill. App. 45, 67 N.E. (2d) 304 (1946).

The early common law courts refused to recognize the trustee in any representative capacity. An action at law against him upon any contract, whether in furtherance of his duties of administration of the trust or not, was personal.[3] A judgment was rendered against him personally, and the party seeking satisfaction was not permitted to levy execution upon the trust property.[4] This early doctrine has been retained in many jurisdictions for a declared purpose of allowing the third party a remedy. Early courts felt that if the trustee were not held to be personally liable, the third party would have difficulty finding a remedy since courts of law did not recognize a trust arrangement. Then, too, the policy considerations of protection of the *cestui's* interest are better main-

[1] Ill. Ann. Stat. (Smith-Hurd, 1935) c. 98, § 40. That section provides "Where the instrument contains, or a person adds to his signature, words indicating that he signs for or on behalf of the principal, or in a representative capacity, he is not liable on the instrument if he was duly authorized. . . ."

[2] The court cited Newby v. Kingman, 309 Ill. App. 36, 32 N.E. (2d) 647 (1941).

[3] This rule of law is widely observed even today. 2 SCOTT, THE LAW OF TRUSTS, § 266 at p. 1500 (1939); 3 BOGERT, THE LAW OF TRUSTS AND TRUSTEES, § 712 (1935); Wolf v. Schiff Trust & Savings Bank, 276 Ill. App. 527 (1934) (tort); Lazenby v. Codman, (D.C. N.Y. 1939) 28 F. Supp. 949; Feldman v. Preston, 194 Mich. 352, 160 N.W. 655 (1916); Kincaid v. Hensel, 185 Wash. 503, 55 P. (2d) 1050 (1936); Taylor v. Davis' Admx., 110 U. S. 330, 4 S. Ct. 147 (1884); O'Brien v. Jackson, 167 N.Y. 31, 60 N.E. 238 (1901); 50 YALE L. J. 1119 (1941); Rowley and Vanneman, "The Uniform Trust Act," 5 OHIO ST. L. J. 145 at 156 (1939); 65 C.J., Trusts, § 744bb(aa), p. 862.

[4] Zehnbar v. Spillman, 25 Fla. 591, 6 S. 214 (1889); Feldman v. Preston, 194 Mich. 352, 160 N.W. 655 (1916); Smith v. Chambers, 117 W. Va. 204, 185 S.E. 211 (1936) [citing 2 TRUSTS RESTATEMENT, § 266 (1935)] Hussey v. Arnold, 185 Mass. 202, 70 N.E. 87 (1904). If the action was against the trustee "as trustee," and his liability was personal, the words "as trustee" were mere surplusage: Alfano v. Donnelly, 285 Mass. 554, 189 N.E. 610 (1934); Odd Fellows Hall Assn. v. McAllister, 153 Mass. 292, 26 N.E. 862 (1891). In many of the code states, however, where law and equity are one, if the action lies against the trustee personally and he is sued "as trustee," such words are not surplusage and the action must be dismissed, being an action against a different person: O'Brien v. Jackson, 167 N.Y. 31, 60 N.E. 238 (1901); Mulrein v. Smillie, 25 App. Div. 135, 48 N.Y. S. 994 (1898); Parmenter v. Barstow, 22 R.I. 245, 47 A. 365 (1900).

tained if the trustee is held personally liable initially.[5] But even though the trustee was personally liable at law, even in cases where the consideration accrued to the estate, he was able to obtain indemnity from the estate if his act were proper and necessary in the administration of the trust.[6] And many courts have come to realize that instead of seeking recovery from the trustee at law, the holder of the instrument or the promisee might in some cases proceed in equity to subject the trust estate to the payment of the claim for which it is liable.[7] The question of permitting a suit in equity against the trustee as such is not dependent upon the juristic personality of the trustee, but upon considerations more exclusively of substantive law—whether a creditor in any given case should be permitted to reach the trust estate.[8] One of the earliest theories advanced for the liability of the trust estate directly to the creditor was that of the application of the creditor for satisfaction out of the estate, upon the basis of subrogation of the trustee's right to exoneration.[9] Here, clearly, the creditor's rights are limited by the trustee's right to indemnity from the estate.[10] Or a creditor might seek satisfaction upon a theory of unjust enrichment of the estate.[11] Or the estate may be found liable upon the basis of the terms of an agreement between the trustee and the promisee, exonerating the trustee individually and dealing with him on the credit of the trust estate.[12] This theory recognizes the liability of the trust estate for its expenses through the exercise by the trustee of his power to appropriate trust property for a trust purpose, as dis-

[5] 3 BOGERT, THE LAW OF TRUSTS AND TRUSTEES, § 712 (1935); Duvall v. Craig, 2 Wheat. (15 U.S.) 45 (1817); O'Brien v. Jackson, 167 N.Y. 31, 60 N.E. 238 (1901). For decisions stating that trustee may not bind his estate by any note or bill, see: Forster v. Fuller, 6 Mass. 58 (1809); Conner v. Clark, 12 Cal. 168 (1859); Hills v. Bannister, 8 Cow. (N.Y.) 32 (1827).

[6] Stone, "A Theory of Liability of Trust Estates for the Contracts and Torts of the Trustee," 22 COL. L. REV. 527 at 531 (1922).

[7] In general, see 2 SCOTT, THE LAW OF TRUSTS, §§ 262-271A.1 (1939).

[8] Whiting v. Hudson Trust Co., 234 N.Y. 394, 138 N.E. 33 (1923). See also 2 SCOTT, THE LAW OF TRUSTS, §§ 267, 271A. (1939).

[9] Stone, "A Theory of Liability of Trust Estates for the Contract and Torts of the Trustee," 22 COL. L. REV. 527 at 536 (1922). Power of creditor to resort to equity to compel the trustee to exercise his power to apply the trust to the payment of proper expenses. Even where the trustee has not stipulated that he will thus exercise his power, equity will compel it for the benefit of a creditor wherever the legal remedies fail, at least where the trustee is not in arrears on his account with the trust estate. 2 SCOTT, THE LAW OF TRUSTS, § 268 (1939); 50 YALE L. J. 1119 (1941).

[10] 2 TRUSTS RESTATEMENT, § 268 (1935); 2 SCOTT, THE LAW OF TRUSTS, § 268.2 (1939).

[11] 2 SCOTT, THE LAW OF TRUSTS, § 269 (1939); 2 TRUSTS RESTATEMENT, § 269 (1935) (application of the doctrine of quasi-contract); Whiting v. Hudson Trust Co., 234 N.Y. 394, 138 N.E. 33 (1923).

[12] 2 TRUSTS RESTATEMENT, § 271 (1935); Jessup v. Smith, 223 N.Y. 203, 119 N.E. 403 (1918), recognizing the power in the trustee to apply the trust funds for proper and necessary expenses (stipulation in the contract that the attorney would look only to the trust estate for his fee); 2 SCOTT, THE LAW OF TRUSTS, § 263 (1939); O'Connell v. Horwich, 284 Ill. App. 554, 1 N.E. (2d) 231 (1936) (No stipulation in contract, but parties shown to have dealt with knowledge of trustee's representative capacity and to have understood him to be free of personal liability).

tinguished from a right of the trustee to compensation or indemnity.[13] Occasionally a creditor has succeeded against the trustee in his representative capacity and gained satisfaction from the trust property when there has been a direct charge upon the estate by virtue of terms incorporated in the trust instrument in the form of an exculpatory clause.[14] The procedural and substantive law difficulties of permitting an action against the trustee as such have been met in four western code states by unique statutes establishing an agency authority for trustees and making their contracts as such directly binding upon the trust estate.[15] Section 20 of the Negotiable Instruments Law and section 12 of the Uniform Trusts Act act as further protection for the trustee. The former excuses the trustee from personal liability if he signs an authorized note or bill in his representative capacity, disclosing his principal.[16] This section more realistically effectuates the trustee's intent to absolve himself from personal liability upon designating himself as trustee of a named estate by changing the general rule that a name, followed by such a designation of relationship, would be considered only *descriptio personae* and the maker therefore would be personally liable.[17] Section 12 of the Uniform Trusts Act extends this representative liability to all contracts, but subsection (3) retains the personal liability of the trustee in certain cases.[18] The modern trend exemplified by these approaches

[13] Stone, "A Theory of Liability of Trust Estates," 22 COL. L. REV. 527 at 535 (1922).

[14] East River Savings Bank v. 245 Broadway Corporation, 284 N.Y. 470, 31 N.E. (2d) 906 (1940), exemption from personal liability on ground of exculpatory clause in trust declaration, to which reference was made in mortgage and bond renewal; as to effect of a provision in a recorded trust agreement exempting trustee from personal liability on the contract, see James Stewart & Co., Inc. v. National Shawmut Bank of Boston, (C.C.A. 1st, 1935) 75 F. (2d) 148, noted in 20 MINN. L. REV. 574 (1936); see also Birdsong v. Jones, 222 Mo. App. 768, 8 S.W. (2d) 98 (1928); 2 TRUSTS RESTATEMENT, § 270 (1935).

[15] "A trustee is a general agent for the trust property. His authority is such as is conferred upon him by the declaration of trust and by this chapter. . . . His acts, within the scope of his authority, bind the trust property to the same extent as the acts of the agent bind his principal." This provision appears in: Cal. Civ. Code (1941) § 2267; Mont. Rev. Code (Anderson & McFarland, 1935) § 7914; N.D. Rev. Code (1943) § 59.0210; S.D. Code (1939) § 59.0209. These statutes have been so construed, however, as to preclude considering the estate as an entity, chargeable as principal for the acts of its trustee, agent; rather, "the legal incidents of the trustee's acts, so far as the parties are concerned, are the same as those which would attach to an agent's authorized transaction for his principal . . . the obligation is clearly that of the trust estate and of the trustee as such, and not of the trustee personally." Tuttle v. Union Bank & Trust Co., 112 Mont. 568, 119 P. (2d) 884 (1941).

[16] N.I.L. was thus applied to the principal case. Negotiable Instruments Law § 20; BRANNON, NEGOTIABLE INSTRUMENTS LAW, 6th ed., § 20, pp. 295, 299 (1938).

[17] See note 4, supra. Tampa Investment & Securities Co. v. Taylor, 272 Ill. App. 541 (1933).

[18] Rowley and Vanneman, "The Uniform Trusts Act," 5 OHIO ST. L. J. 145 (1939). Here, too, the decisions are to the effect that the addition of words such as "trustee" and "as trustee" are prima facie evidence of "an intent to exclude the trustee from personal liability" [U.T.A. § 12 (3)] and no longer mere *descriptio personae.*

gives the third party a claim enforceable against the trust estate. In effect, it personifies the estate, recognizing equitable suit or civil action against the trustee in his representative capacity.

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