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THE TRUST POWERS OF NATIONAL BANKS

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Prior to December 23, 1913, national banks possessed no trust powers. They could not act as fiduciaries. On that date the *Federal Reserve Act* became law.¹ It created a Federal Reserve Board and granted to that board, *inter alia*, the power to permit national banks to engage in trust activities.² The constitutionality of the *Federal Reserve Act* was challenged in 1915, in Illinois, on the ground that the establishment of the Federal Reserve Board was a delegation of legislative power.³ The challenge was not successful. It was determined that the giving of the powers to the Federal Reserve Board constituted a delegation, not of legislative, but of administrative functions. As such, there was a valid grant of powers to the Federal Reserve Board. But the court held that Congress could not give national banks the privilege of acting as fiduciaries because such a privilege was not necessary to maintaining the efficiency of the national banks as governmental agencies. This, according to the Illinois court, was proved by the fact that Congress left the exercise of fiduciary

¹ 38 STAT. 251, c. 6 (1913), 12 U. S. C. c. 3 (1926).

² 38 STAT. 260, § 10 (1913), 12 U. S. C. §§ 241-247 (1926); 38 STAT. 262, § 11 (k) (1913), 12 U. S. C. § 248 (k) (1926).

³ *People v. Brady*, 271 Ill. 100, 110 N. E. 864 (1915).

functions to the discretion of the national bank, and did not order all national banks to operate as fiduciaries. Two years later, however, the United States Supreme Court held that the giving of trust powers to national banks by Congress was constitutional.⁴ This settled the question of the constitutionality of the powers exercised by the Federal Reserve Board under the *Federal Reserve Act*. National banks derive their trust powers from Congress, and may exercise them after they have received permission to do so from the Federal Reserve Board.

I. THE ACQUISITION OF TRUST POWERS

Before a national bank can exercise trust powers it must receive a special permit to do so.⁵ Formal application⁶ must be made for the permit. This application must name the state and the federal reserve district in which the bank is located. It must contain a request for the special permit, and show that the application is being made under a valid resolution of the board of directors of the applicant bank. A copy of the resolution, duly certified by the secretary or cashier of the applicant bank, must accompany the application. The application must be executed under the seal of the bank, signed by the president or vice-president of the bank, and attested by the secretary or cashier. It must also contain a statement of the financial condition of the bank as of the close of the business day on the date of application. Assets and liabilities must be listed. Of particular importance are the items of capital and surplus. These sway the discretion of the Federal Reserve Board when considering the application. The application must be addressed to the Federal Reserve Board. It is mailed, however, to the chairman of the board of directors of the federal reserve bank of the district in which the applicant bank is located. It is his duty to transmit the

⁴ *National Bank of Bay City v. Fellows*, 244 U. S. 416, 37 Sup. Ct. 734 (1917).

⁵ Federal Reserve Act, *supra* note 2, § 11 (k); REGULATIONS OF THE FEDERAL RESERVE BOARD (1928) 27, reg. F, hereinafter cited "Reg. 1928F."

⁶ There are two application forms. Form 61 is used when the request is first made for fiduciary powers. Form 61b is used when additional fiduciary powers are wanted by a bank which has already been permitted to exercise some powers.

application to the Federal Reserve Board.⁷ The Federal Reserve Board has complete discretion in the granting of the permit. It considers each application in the light of the needs of the community within which the applicant bank is situated, the amount of the capital and surplus, the sufficiency of the capital and surplus to assure a safe discharge of the trust powers if granted, and any other facts and circumstances which come to its notice. A national bank is not entitled to the permit as a matter of right. There are two negative restrictions upon the powers of the Federal Reserve Board in granting the permit. (1) If the capital and surplus of the applicant bank are less than the capital and surplus which is required of state banks, trust companies or other corporations exercising trust powers within that state, by the law of the state in which the applicant bank is located, the Federal Reserve Board cannot issue the permit to the applicant bank.⁸ (2) If the right to exercise trust powers on the part of the applicant bank would be in "contravention of State or local law" the Federal Reserve Board cannot issue the permit to the applicant bank.⁹

Nine classes of trust powers may be permitted to the national bank. These are "the right to act as": (1) a trustee; (2) an executor; (3) an administrator; (4) a registrar of stocks and bonds; (5) a guardian of estates; (6) an assignee; (7) a receiver; (8) a committee of estates of lunatics; and (9) "any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located".¹⁰

One of four situations may exist at the time the permit is requested:

1. A group may be organizing a new national bank. In this case the application may be made by the organizers on behalf of the new national bank, in advance of the completion of the

⁷ Form 61, n.

⁸ Federal Reserve Act, *supra* note 2, § 11 (k), last par.

⁹ Federal Reserve Act, *supra* note 2, § 11 (k), par. 1.

¹⁰ Federal Reserve Act, 40 STAT. 968, § 2 (1918), 12 U. S. C. § 248 (k) (1926).

organization. The permit will be issued simultaneously with the completion of the organization in the name of the newly organized national bank.

2. A state bank or trust company may be converted into a national bank. The state bank or trust company may apply in advance for the permit, on behalf of the national bank into which it is to be converted. The permit will be issued simultaneously with the completion of the conversion.

3. Two or more national banks may consolidate. (a) If none of these banks has already received a permit to act as a fiduciary, the application may be made, in advance of the consolidation and on behalf of the consolidated bank, by the national bank whose charter is to be retained by the consolidated bank. The permit will be issued simultaneously with the completion of the consolidation. (b) If one of the consolidating banks has received a permit prior to the consolidation, the right to exercise trust powers under that permit passes, by operation of law, to the consolidated bank. The consolidated bank may exercise such powers as were possessed by the bank which originally received the permit. But the Federal Reserve Board thinks it advisable that the consolidated bank should have a permit in its own name. This would keep the records of the consolidated bank clear, and would avoid any possible question concerning the right of the consolidated bank to exercise trust powers. The permit may be applied for in the name of the consolidated bank, by the bank whose charter is to be retained, in advance of the consolidation. The permit will be issued in the name of the consolidated bank. It will take effect when the consolidation is completed.

4. A state bank or trust company may consolidate with a national bank under the charter of the national bank. In this case the application for the permit should be made by the national bank on behalf of the consolidated national bank. The application may be made in advance. The permit will be issued simultaneously with the consummation of the consolidation.¹¹

¹¹ Reg. 1928F, § ii.

II. THE EXERCISE OF TRUST POWERS BY A NATIONAL BANK

The trust powers of a national bank were originally conferred by the *Federal Reserve Act* in a provision which read as follows:

"To grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator or registrar of stocks and bonds, under such rules and regulations as the said board may prescribe." ¹²

This act did not give the national banks the unqualified privilege to exercise trust powers. The phrase "when not in contravention of State or local law" was a limitation upon the powers. The phrase "local law" is an odd one. It does not mean "state law". If the laws of the several territories of the United States and of the District of Columbia are to be dealt with as though they were "state laws", which is the usual procedure, then the phrase "local laws" does not refer to the statutes of the territories or the District of Columbia. It must refer to the ordinances of cities or other territorial subdivisions of the several states. That is, it refers to the legislative enactments of municipal corporations. If the phrase "local law" does not refer to the enactments by municipal corporations, it must refer to legislation by insular possessions of the United States. It may, of course, refer to both. So far as the writer has been able to ascertain, no case has, as yet, dealt with the meaning of the phrase "local law". "State law", of course, refers to the legislative enactments of the several states.

When, in pursuance of the above section of the *Federal Reserve Act*, the Federal Reserve Board granted permits to some national banks to exercise trust powers, the powers of these national banks were promptly challenged. The basis of the challenge was the phrase "when not in contravention of State or local law". The argument was advanced that the national banks could not do what the state law did not permit.

¹² *Supra* note 2, § 11 (k).

In 1915 a national bank in Illinois, having received permission from the Federal Reserve Board to act as a trustee, asked authority from the auditor of Illinois to be allowed to exercise its powers in Illinois. The authority was refused on the ground that the control of property within a state was a function of state law, and that national law could not apply. Suit was brought by the bank. The question was whether or not the powers granted to the national bank by the Federal Reserve Board were "in contravention of State law". The court held that they were, saying that trusteeships and executorships were the instrumentalities of the state law; that the control of property within a state was a function of the law of that state; and that Congress had no power to exercise control over property within the borders of the state.¹³

In the same year, in New Hampshire, a similar decision was rendered. The New Hampshire statute provided that:

"No trust company, loan and trust company, bank or banking company or similar corporation shall hereafter be appointed administrator of an estate, executor under a will, or guardian or conservator of the person or property of another." ¹⁴

A national bank petitioned to be appointed administrator of an estate. The petition was refused by the probate court. An appeal was taken from the decision of the probate judge to the supreme court of the state. The question was whether the section of the *Federal Reserve Act* which gave the national bank power to act as administrator superseded the state law so far as the national bank was concerned. The court, holding that it did not, said:

"The statute (of the state) does not attempt to manage or regulate the business of national banks located within the state in contravention of the laws of the United States, . . . but it merely prohibits the probate courts from appointing them to act as administrators, executors or guardians. Moreover, the federal reserve act recognizes the right

¹³ *People v. Brady*, *supra* note 3.

¹⁴ N. H. Laws 1915, § 34.

of the state to prevent banks from acting in those capacities, and grants them the power to do so only 'when not in contravention of state or local law'. As the exercise of such power is in contravention of our statute the appointment of the bank would be illegal." ¹⁵

The court further held that Congress had no power to tell a probate court of the State of New Hampshire what that court should do, and that national banks have no vested right to be appointed as fiduciaries, nor to act as fiduciaries unless properly appointed as such by the law of New Hampshire.

Neither of these cases was carried to the United States Supreme Court. But the next year a case arose which was so carried. The law of Michigan forbade national banks from doing business as trust companies. The First National Bank of Bay City received permission from the Federal Reserve Board to act as a fiduciary. It began to exercise trust powers. A trust company protested to the attorney general of the state against the activities of the national bank. The attorney general brought suit against the national bank, in the nature of *quo warranto* proceedings, to stop the trust activities of the national bank. The national bank defended on the ground that it had received its powers from the Congress of the United States. The Supreme Court of the State of Michigan, however, held that Congress was without authority to grant trust powers to national banks, that the laws of the state forbade the exercise of trust powers by national banks, and that the exercise of such powers would be in contravention of the laws of the state. The national bank appealed to the Supreme Court of the United States, which decided in favor of the national bank. Mr. Chief Justice White wrote the opinion. His language is so far-reaching as to merit quotation in full. He said, after referring to the cases of *McCulloch v. Maryland* ¹⁶ and *Osborn v. Bank*: ¹⁷

"What those cases established was that although a business was of a private nature and subject to state regulation,

¹⁵ Woodbury's Appeal, 78 N. H. 50, 52, 96 Atl. 299, 300 (1915).

¹⁶ 4 Wheat. 316 (U. S. 1819).

¹⁷ 9 Wheat. 738 (U. S. 1824).

if it was of such a character as to cause it to be incidental to the successful discharge by a bank chartered by Congress of its public functions, it was competent for Congress to give the bank the power to exercise such private business in co-operation with or as part of its public authority. Manifestly this excluded the power of the state in such case, although it might possess in a general sense authority to regulate such business, to use that authority to prohibit such business from being united by Congress with the banking function, since to do so would be but the exertion of state authority to prohibit Congress from exerting a power which under the Constitution it had a right to exercise. From this it must also follow that even although a business be of such a character that is not inherently susceptible of being included by Congress in the powers conferred on national banks, that rule would cease to apply if by state law state banking corporations, trust companies, or others which by reason of their business are rivals or *quasi*-rivals of national banks are permitted to carry on such business. This must be since the State may not by legislation create a condition as to a particular business which would bring about actual or potential competition with the business of national banks and at the same time deny the power of Congress to meet such created condition by legislation appropriate to avoid the injury which otherwise would be suffered by the national agency. Of course as the general subject of regulating the character of business just referred to is peculiarly within state administrative control, state regulations for the conduct of such business, if not discriminating or so unreasonable as to justify the conclusion that they necessarily would so operate, would be controlling upon banks chartered by Congress when they came in virtue of authority conferred upon them by Congress to exert such particular powers. And these considerations were clearly in the legislative mind when it enacted the statute in question. This result would seem to be plain when it is observed (a) that the statute authorizes the exertion of the particular functions by national banks when not in contravention of the state law, that is, where the right to perform them is expressly given by the state law or what is equivalent is deducible from the state law because that law has given the functions to state banks or corporations whose business in a greater or less degree rivals that of national banks, thus engendering from the state law itself an implication of authority in Congress to do as to national

banks that which the state law has done as to other corporations; and (b) that the statute subjects the right to exert the particular functions which it confers on national banks to the administrative authority of the Reserve Board, giving besides to that Board power to adopt rules regulating the exercise of the functions conferred, thus affording the means of coördinating the functions when permitted to be discharged by national banks with the reasonable and non-discriminatory provisions of state law regulating their exercise as to state corporations—the whole to the end that harmony and the concordant exercise of the national and state power might result.”¹⁸

This case clearly lays down the following propositions:

1. Congress has the authority to confer trust powers upon national banks as an incident of their governmental functioning.

2. The exercise of those powers is subject to the rules and regulations of the Federal Reserve Board, and to the rules and regulations of the state within which the national bank wishes to exercise its trust powers.

3. The rules and regulations of the state must apply equally to national banks and to all other corporations permitted by the state to exercise trust powers.

4. The rules and regulations of the state must be reasonable, and must not operate, in fact and result, to discriminate against the national banks in any way. Where the practical effect of a rule or regulation is to inhibit or impede the exercise of trust powers by national banks, that rule or regulation is invalid.

5. A national bank may exercise, within a state, such trust powers as the laws of the state, expressly or by implication, permit any corporation which is in any way a rival and competitor of the national bank to exercise. The state by giving powers to state corporations gives them, *ipso facto*, to a national bank within the state.

Following the decision in the *Fellows* case, Congress amended the *Federal Reserve Act*.¹⁹ It increased, among other

¹⁸ *National Bank of Bay City v. Fellows*, *supra* note 4, at 425-427, 37 Sup. Ct. at 737-738, *rev'g*, 192 Mich. 640, 159 N. W. 335 (1916).

¹⁹ Act of September 26, 1918, 40 STAT. 967, c. 177 (1918), 12 U. S. C. c. 3 (1926).

things, the trust powers of national banks. The *Federal Reserve Act* now gives the Federal Reserve Board authority

"to grant by special permit to national banks applying therefor, when not in contravention of State or local law, the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, committee of estates of lunatics, or in any other fiduciary capacity in which State banks, trust companies, or other corporations which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located.

"Whenever the laws of such State authorize or permit the exercise of any or all the foregoing powers by State banks, trust companies, or other corporations which compete with national banks, the granting to and the exercise of such powers by national banks shall not be deemed to be in contravention of State or local law within the meaning of this Act." ²⁰

This amendment is a clear acceptance by Congress of the decision in the *Fellows* case. It makes actual or potential competition by state corporations the test of the right of a national bank to exercise the trust powers given to them by the Federal Reserve Board.

Notwithstanding the foregoing amendment to the *Federal Reserve Act*, and the *Fellows* case, the Missouri courts were not yet persuaded that state law could be rendered inoperative by Congressional action when dealing with national banks. In 1924 the Supreme Court of Missouri considered the case of *State v. Duncan*.²¹ In that case X died leaving a will in which he named the Burnes National Bank as executor. At that time the law of Missouri was that national banks were not qualified to act as executors. The Burnes National Bank applied to the probate court for letters testamentary. The court refused the request on the ground that national banks were precluded by state law from being executors. The bank applied to the Supreme Court of the State of Missouri for a writ of mandamus directed to the judge of the probate court. An alternative writ was issued. The re-

²⁰ 40 STAT. 968, § 2 (1918), 12 U. S. C. § 248 (k) (1926).

²¹ *State ex rel. Burnes Nat. Bank v. Duncan*, 302 Mo. 130, 257 S. W. 784 (1924).

spondent demurred. The demurrer was sustained and a peremptory writ was denied. A writ of error was allowed by the Chief Justice of the Supreme Court of the State of Missouri, and the matter was taken to the Supreme Court of the United States. The sole question to be decided was this: has the national bank authority to be an executor under the *Federal Reserve Act*? The answer was given in the affirmative. Mr. Justice Holmes wrote the decision. He adopted the *Fellows* case, and said:

"The question is pretty nearly answered by the decision and fully answered by the reasoning in the *First National Bank of Bay City v. Fellows*, 244 U. S. 416. That case was decided before the amendment of the Federal Reserve Act that we have quoted and came here on the single issue of the power of Congress when the State law was not contravened. It was held that the power 'was to be tested by the right to create the bank and the authority to attach to it that which was relevant in the judgment of Congress to make the business of the bank successful.' 244 U. S. 420. The power was asserted and it was added that 'this excluded the power of the State in such case, although it might possess in a general sense authority to regulate such business, to use that authority to prohibit such business from being united by Congress with the banking function.' 244 U. S. 425. Now that Congress has expressed its paramount will this language is more apposite than ever. The States cannot use their most characteristic powers to reach unconstitutional results. . . . There is nothing over which a State has more exclusive authority than the jurisdiction of its courts, but it cannot escape its constitutional obligations by the device of denying jurisdiction to courts otherwise competent. . . . So here—the State cannot lay hold of its general control of administration to deprive national banks of their powers to compete that Congress is authorized to sustain.

"The fact that Missouri has regulations to secure the safety of trust funds in the hands of its trust companies does not affect the case. The power given by the act of Congress purports to be general and independent of that circumstance and the act provides its own safeguards. The authority of Congress is equally independent, as otherwise the State could make it nugatory. . . ." ²²

²² State *ex rel.* Burnes Nat. Bank v. Duncan, 265 U. S. 17, 23-24, 44 Sup. Ct. 427, 428 (1924).

It cannot be doubted that this decision is definitive. And various rules of law may be asserted as established with certainty. A national bank is a federal agency.²³ It is subject to the control of federal law and is independent of state control,²⁴ unless Congress expressly places the control in the hands of the states.²⁵ A state cannot interfere with a national bank,²⁶ nor withhold from the national bank any powers which Congress has given to that bank.²⁷ The laws of a state dealing with national banks are subservient to the acts of Congress;²⁸ and, as the Federal Reserve Board is an administrative arm of Congress,²⁹ the regulations of the Federal Reserve Board concerning national

²³ *Easton v. Iowa*, 188 U. S. 220, 23 Sup. Ct. 288 (1903); *State ex rel. Burnes Nat. Bank v. Duncan*, *supra* note 22; *First Nat. Bank of St. Louis v. State*, 263 U. S. 640, 44 Sup. Ct. 213 (1924); *Tarrant v. Bessemer Nat. Bank*, 7 Ala. App. 285, 61 So. 47 (1913); *Myers v. Exchange Nat. Bank*, 96 Wash. 244, 164 Pac. 951 (1917); see *Christopher v. Nowell*, 201 U. S. 216, 225, 26 Sup. Ct. 502, 505 (1905).

²⁴ *McCulloch v. Maryland*, *supra* note 16; *Davis v. Elmira Sav. Bank*, 161 U. S. 275, 16 Sup. Ct. 502 (1895); *Clement Nat. Bank v. Vermont*, 231 U. S. 120, 34 Sup. Ct. 31 (1913); *National Bank v. Murray*, 212 Fed. 140 (C. C. A. 8th, 1914); *First Nat. Bank v. State*, 262 U. S. 366, 43 Sup. Ct. 602 (1923); *Steele v. Randall*, 19 F.(2d) 40 (C. C. A. 8th, 1927); *Steward v. Atlantic Nat. Bank*, 27 F. (2d) 224 (C. C. A. 9th, 1928); *McClelland v. Nat. Bank*, 77 Colo. 302, 236 Pac. 774 (1925); *Hamilton v. State*, 94 Conn. 648, 110 Atl. 54 (1920); *Hansford v. Nat. Bank*, 10 Ga. App. 270, 73 S. E. 405 (1912); *First Nat. Bank v. Amer. Nat. Bank*, 173 Mo. 153, 72 S. W. 1059 (1903); *State v. First Nat. Bank*, 297 Mo. 397, 249 S. W. 619 (1923); *Montana Nat. Bank v. Yellowstone County*, 252 Pac. 876 (Mont. 1926); *In re Mollineaux*, 109 Misc. 75, 179 N. Y. Supp. 90 (1919); *North Shaker Co. v. Harriman Nat. Bank*, 22 Ohio App. 487, 153 N. E. 909 (1926); *Columbia Nat. Bank v. Powell*, 265 Pa. 85, 108 Atl. 445 (1919); *In re Turner's Estate*, 277 Pa. 110, 120 Atl. 701 (1923); *In re Cameron*, 287 Pa. 560, 135 Atl. 295 (1926); *Aquidneck Nat. Bank v. Jennings*, 44 R. I. 435, 117 Atl. 743 (1922); *First Nat. Bank v. Walton*, 50 S. D. 40, 208 N. W. 221 (1926); *Citizens' Nat. Bank v. Stevenson*, 231 S. W. 364 (Tex. Comm. App. 1921); *Wray v. Citizens' Nat. Bank*, 282 S. W. 659 (Tex. Civ. App. 1926); *Matter of Stanchfield*, 171 Wis. 553, 178 N. W. 310 (1920); *Brust v. First Nat. Bank*, 184 Wis. 15, 198 N. W. 749 (1924).

²⁵ *People v. Godfogle*, 242 N. Y. 277, 151 N. E. 452 (1926), especially concurring opinion of Crane, J., at 398, 151 N. E. at 463.

²⁶ *McCulloch v. Maryland*, *supra* note 16; *First Nat. Bank v. State*; *North Shaker Co. v. Harriman Nat. Bank*; *First Nat. Bank v. Walton*; *Brust v. First Nat. Bank*; *Columbia Nat. Bank v. Powell*; *First Nat. Bank v. Amer. Nat. Bank*, all *supra* note 24; *First Nat. Bank of St. Louis v. State*; *Easton v. Iowa*; *Myers v. Exchange Nat. Bank*, all *supra* note 23; *Fidelity Nat. Bank v. Enright*, 264 Fed. 236 (W. D. Mo. 1920); *Federal Land Bank v. Cosland*, 261 U. S. 374, 43 Sup. Ct. 385 (1922).

²⁷ *McCulloch v. Maryland*, *supra* note 16; *Steward v. Atlantic Nat. Bank*; *Hamilton v. State*, both *supra* note 24.

²⁸ *Fidelity Nat. Bank v. Enright*, *supra* note 26.

²⁹ *People v. Brady*, *supra* note 3.

banks supersede state laws dealing with them.³⁰ It follows, then, that a state cannot add powers to a national bank,³¹ nor can a national bank submit voluntarily to the provisions of a state law if that law is inconsistent with federal laws.³² The state cannot impose criminal penalties upon a national bank,³³ nor impose any liabilities upon the national bank which grow out of powers given to the national bank by the state itself in derogation of federal law.³⁴ The criminal law of a state does not apply to national banks.³⁵ Nor does the state law concerning torts.³⁶ But where the acts of a national bank are *ultra vires*, the law of the state within whose territory the acts occurred controls those acts.³⁷

It follows from the foregoing that if a national bank located within a state receives permission to exercise trust powers from the Federal Reserve Board, it may exercise such powers within the state in spite of the existence of state laws to the contrary.³⁸ This is so in spite of the caution expressed by the Federal Reserve Board when it states that its regulations must not be construed to give a national bank "rights or privileges in contravention of the laws of the State in which the bank is located within the meaning of" the *Federal Reserve Act*.³⁹ Hence a national bank may act as

³⁰ *In re Turner's Estate*, *supra* note 24.

³¹ *Myers v. Exchange Nat. Bank*, *supra* note 23, at 255, 164 Pac. at 955.

³² *In re Turner's Estate*, *supra* note 24.

³³ *Curtis v. Western Reporting & Credit Co.*, 39 Idaho 784, 230 Pac. 771 (1924).

³⁴ *Myers v. Exchange Nat. Bank*, *supra* note 23.

³⁵ *Easton v. Iowa*, *supra* note 23; *State v. Menke*, 56 Kan. 77, 42 Pac. 350 (1896); *Stout v. Lusk*, 9 Kan. App. 694, 59 Pac. 603 (1899); *Comm. v. Felton*, 101 Mass. 204 (1869); *People v. Fonda*, 62 Mich. 401, 29 N. W. 26 (1886); *Comm. v. Ketner*, 92 Pa. 373 (1880); *Allen v. Carter*, 119 Pa. 192, 13 Atl. 70 (1888). There is a suggestion to the contrary in *State v. Fields*, 98 Iowa 748, 62 N. W. 653 (1896).

³⁶ *Hansford v. Nat. Bank*, *supra* note 24; *Roberts v. Nat. Bank*, 10 Ga. App. 272, 73 S. E. 407 (1912).

³⁷ *First Nat. Bank of St. Louis v. State*, *supra* note 23.

³⁸ *National Bank of Bay City v. Fellows*, *supra* note 4; *In re Turner's Estate*; *McClelland v. Nat. Bank*; *Steele v. Randall*; *Steward v. Atlantic Nat. Bank*; *Hamilton v. State*; *National Bank v. Murray*; *Wray v. Citizens' Nat. Bank*; *In re Cameron*; *Citizens' Nat. Bank v. Stevenson*; *Matter of Stanchfield*, all *supra* note 24; *Easton v. Iowa*; *First Nat. Bank of St. Louis v. State*; *Myers v. Exchange Nat. Bank*, all *supra* note 23; *Commonwealth Atl. Nat. Bank Petition*, 249 Mass. 440, 144 N. E. 443 (1924).

³⁹ Reg. 1918F, § xiv.

a trustee,⁴⁰ an executor,⁴¹ an administrator,⁴² a guardian of an infant,⁴³ or utilize any other trust power which is lawfully exercised by any corporation within the state and under the laws of the state in which the national bank is located.

The phrase "within which the national bank is located" raises the interesting question: where is a national bank located?

The federal banking laws provide that the organizers of a national bank shall specifically state, in the organization certificate:

"The place where its operations of discount and deposit are to be carried on, designating the State, Territory or District, and the particular county and city, town or village." ⁴⁴

This does not mean, however, that the operations of deposit and discount establish the "domicile" of a national bank.⁴⁵ Ordinarily a corporation has its domicile in the state where it has been incorporated.⁴⁶ But a national bank is not incorporated by any state. It is created by the United States. If a national bank has any domicile at all it must be domiciled throughout the United States. Or else it must be domiciled in the District of Columbia where the seat of the federal government is situated. If a national bank is domiciled in the District of Columbia, or if a national bank is domiciled in the state "where its operations of deposit and discount are to be carried on", then it might be argued that a national bank "is located" only in the District of Columbia

⁴⁰ *Carpenter v. Aquidneck Nat. Bank*, 46 R. I. 152, 125 Atl. 358 (1924); *North Shaker Co. v. Harriman Nat. Bank*, *supra* note 24.

⁴¹ *State ex rel. Burnes Nat. Bank v. Duncan*, *supra* note 22; *Carpenter v. Aquidneck Nat. Bank*, *supra* note 40; *Commonwealth Atl. Nat. Bank Petition*, *supra* note 38; *Matter of Stanchfield*, *supra* note 24.

⁴² *Woodbury's Appeal*, *supra* note 15.

⁴³ *In re Turner's Estate*; *Hamilton v. State*; *In re Mollineaux*, all *supra* note 24.

⁴⁴ R. S. § 5134, 12 U. S. C. § 22 (1926). This section was derived from the Act of June 3, 1864, c. 106, § 6, 13 STAT. 101.

⁴⁵ MINOR, *CONFLICT OF LAWS* (1901) 129; GOODRICH, *CONFLICT OF LAWS* (1927) 61; *Baty, The Right of Ideas—and of Corporations* (1920) 33 HARV. L. REV. 358, 370.

⁴⁶ *O. & M. R. R. v. Wheeler*, 66 U. S. 286 (1861); *Beale, Foreign Corporations* (1904) § 71; MINOR, *op. cit. supra* note 45, at 130; GOODRICH, *op. cit. supra* note 45, at 61.

or in the state where the operations of discount and acceptance of deposits are carried on. If that is true, then a national bank would be a "foreign corporation" in any other state. And it has been so held.⁴⁷ But it has also been held that a national bank is a domestic and not a foreign corporation,⁴⁸ even though the national bank has its place of discount and deposits in another state.⁴⁹ It is submitted that the second is the better view. A government agency cannot be said to exist in only a segment of the federal territory. A federal charter to do a national banking business cannot be deemed to restrict the operations of the national bank to a single state, nor to locate that bank in a single state. It is for this reason that a national bank does not need a state license to do business in any state.⁵⁰ It is this which distinguishes a national bank from a foreign corporation doing business in a state under a license from that state.⁵¹ A state, therefore, cannot keep a national bank outside of its borders,⁵² nor prevent a national bank from carrying on business within its territory.⁵³ And necessarily this would be true of the trust activities of a national bank as well as of its other activities. Hence it would seem to be clear that no state can place restrictions upon the solicitation of business by the trust department of a national bank within its territory. For example, there is a statute in New Jersey which prohibits national banks located in other states from soliciting trust business in New Jersey.⁵⁴ National banks in New York, consequently, do not send their solicitors for trust business into New Jersey. There can be no question but that the New Jersey statute is null and void so far as national banks are concerned. The soliciting of trust business is a necessary part of the activities of a trust department in a national bank. The New Jersey statute purports to control and direct such solicitation.

⁴⁷ *North Shaker Co. v. Harriman Nat. Bank*, *supra* note 24.

⁴⁸ *Hummel v. First Nat. Bank*, 2 Colo. App. 571, 32 Pac. 72 (1892); *Market Nat. Bank v. Pac. Nat. Bank of Boston*, 64 How. Prac. 1 (N. Y. 1882).

⁴⁹ *Steward v. Atlantic Nat. Bank*, *supra* note 24.

⁵⁰ *Brust v. First Nat. Bank*, *supra* note 24.

⁵¹ *Brust v. First Nat. Bank*, *supra* note 24.

⁵² *Brust v. First Nat. Bank*, *supra* note 24, at 22, 198 N. W. at 752.

⁵³ *Brust v. First Nat. Bank*, *supra* note 24.

⁵⁴ N. J. Pub. Laws 1907, p. 68.

The regulation impedes and interferes with the business of the national bank. Furthermore, the state banks and the trust companies of New Jersey are in definite and keen competition with the national banks of New York. The law is clear that state or local discrimination in favor of competitors or quasi-competitors of national banks must not be made. Such discriminatory legislation is obviously invalid. National banks may safely ignore it.⁵⁵ A national bank by virtue of its federal charter may enter any state, and engage in any activities permitted by its charter powers within the territory of that state, provided such activities are reasonably necessary for the carrying on of its business as a national bank in competition with the banks, trust companies or other corporations within that state.

During the past fifteen years there has been an extraordinary expansion of banking business. This expansion has been marked by huge mergers and consolidations of banks and trust companies. It was inevitable that some questions concerning the exercise of trust powers by the consolidated banks should arise. There were four situations: (1) where a national bank permitted to exercise trust powers united with another bank also permitted to exercise trust powers; (2) where a national bank permitted to exercise trust powers united with a national bank which did not have permission to exercise trust powers; (3) where a national bank permitted to exercise trust powers united with a trust company; (4) where a national bank which did not have permission to exercise trust powers united with a trust company. And in each situation the problem was twofold: (a) in regard to trust activities already being carried on; and (b) in regard to future trust activities.⁵⁶

1. If the consolidating national banks had permission to exercise trust powers, that permission passed by operation of law to the consolidated organization, so that all trust activities, both present and future, of all the banks, could be carried on by the consolidated bank.⁵⁷

⁵⁵ This is the irrefutable result of the logic of the Fellows and Duncan cases, *supra* notes 18, 21 and 22.

⁵⁶ Reg. 1928F, §§ iii, iv.

⁵⁷ *Ibid.* § iii.

2. If only one of the consolidating national banks had permission to exercise trust powers, that permission passed by operation of law to the consolidated bank, so that all present and future trust activities of the consolidating bank which had permission to carry on a trust business passed to the consolidated bank. And, of course, the consolidated bank had permission to carry on future trust activities.⁵⁸

3. If the national bank which consolidated with a trust company had authority to exercise trust powers, it is clear that all present trust activities of the national bank could be carried on by the consolidated bank. This would be so because the permission of the national bank to exercise trust powers passed by operation of law to the consolidated bank. But this would not necessarily be true of the trust powers of the trust company. The creator of a trust may have had complete faith in the trust company as a trustee, while he might not have had any faith in the national bank as a trustee, and may not have intended the consolidated bank to be the successor trustee of the trust company. The successor trustee is not, in contemplation of law, the same person as the original trust company. The laws of the state which controlled the operations of the trust company might not permit consolidated national bank-trust companies to act as successor trustees. In that case the consolidated bank would not be permitted to take over the existing trust business of the consolidating trust company. As to the future trust business of the trust company, it would be quite clear that the consolidated bank was not the trust company, and so would not be permitted to become the trustee under a will, for example, which specifically named the trust company as trustee. The trust company would no longer exist. The consolidated national bank was not named in the will. Hence neither could act as trustee.

4. The immediately foregoing reasoning is particularly applicable to the situation where the national bank did not have permission to exercise trust powers prior to its consolidation with a trust company. The present trust business of the trust company

⁵⁸ *Ibid.*

might pass to the consolidated national bank if the consolidated national bank received its permit to exercise trust powers simultaneously with the consummation of the consolidation. But the future business of the trust company could not possibly pass to the consolidated national bank. This matter was squarely raised, and decided, in the case of *Commonwealth Atl. Nat. Bank Petition*.⁵⁹ In that case X made a will in which he named the T trust company as executor. Thereafter the T trust company converted itself into a national bank. Following the conversion the converted trust company consolidated with the C national bank. Then X died. The C national bank asked to be appointed executor under X's will. The question was: is the C national bank the proper executor under the will? The court held that it was not. The T trust company had not survived the nationalization process. And the C national bank had not been named in the will. This case cannot be questioned. It is entirely sound in law.

Three years after the decision in the *Commonwealth Bank* case, Congress passed an amendment to the banking laws which made it clear that the consolidated national bank was to have the full power to carry on both the present and future trust business of all the consolidating units. The statutes now provide that when the consolidation is effected

"all the rights, franchises, and interests of such State or District bank so consolidated with a national banking association in and to every species of property, real, personal, and mixed, and choses in action thereto belonging, shall be deemed to be transferred to and vested in such national banking association into which it is consolidated without any deed or other transfer, and the said consolidated national banking association shall hold and enjoy the same and all rights of property, franchises, and interests including the right of succession as trustee, executor, or in any other fiduciary capacity in the same manner and to the same extent as was held and enjoyed by such State or District bank so consolidated with such national banking association. . . . The words 'State bank', 'State banks', 'bank', or 'banks', as used in this section, shall be held to include trust companies, sav-

⁵⁹ *Supra* note 38.

ings banks, or other such corporations or institutions carrying on the banking business under the authority of State laws." ⁶⁰

Within a month after the passing of this amendment the Comptroller of the Currency said:

"I am of the opinion that where a State trust company consolidates with a national bank, such national bank may not only continue to handle all the trust business actually on the books of the trust company at the time of the consolidation but is also legally entitled to be appointed to act as executor, trustee, etc., under wills executed prior to the consolidation naming the trust company to act in such capacities, even where such wills were not admitted to probate until after the consolidation." ⁶¹

It can now hardly be doubted that under the present statutes a consolidated national bank may take over all the trust business, present and future, in which any one of the consolidating units could have engaged had it not entered into the consolidated organization. ⁶²

III. RESTRICTIONS UPON NATIONAL BANKS AS FIDUCIARIES.

A national bank which receives permission to exercise trust powers must, in order to take advantage of that permission, create a trust department which must be separate and apart from the other departments of the bank. ⁶³ The department must be placed in the management of special officers. The duties of the officers must be prescribed by the directors of the bank. The department can be created either by an amendment to the by-laws of the bank, or by a special resolution properly entered upon the minutes of the board of directors.

⁶⁰ Act of February 25, 1927, 44 STAT. 1224, § 1 (1927), 12 U. S. C. § 34a (1928).

⁶¹ Letter of Comptroller of Currency relating to trust powers of national banks, March 22, 1927, FOURTEENTH ANNUAL REP. FED. RES. BOARD, 267-271.

⁶² The Massachusetts courts have decided against the position here taken. *In re Legnard's Estate*, 162 N. E. 217 (Mass. 1928); *cf. In re Parson's Estate*, 161 N. E. 797 (Mass. 1928). It is submitted, however, that *In re Legnard's Estate* is wrongly decided.

⁶³ Reg. 1928F, § v.

The trust department must maintain a separate set of books. These books are subject to examination by federal authorities under the banking laws of the United States. They may also be examined by proper officials of the state within which the bank is located to the same extent that state banks and trust companies are subject to inspection. Such state inspection, however, is limited to the books of the trust department of the national bank only. That the national bank has a trust department does not give authority to the state officials to investigate the books of the national bank which are not connected with the bank's trust business.⁶⁴

The trust assets of the trust department must be completely segregated from all the other assets of the bank. No collection or exchange business can be carried on in the trust department. Nor can a general banking business be done therein. Furthermore, the securities and the investments of each trust must be kept segregated from the securities and investments owned by the bank itself. And the various trust funds must be kept separate from each other. All trust securities must be placed in the joint custody of two or more officers or employees of the bank, designated by the board of directors and properly bonded.⁶⁵

The trust funds secured by the trust department are of two classes: (1) funds received for distribution; and (2) funds received for investment. The funds which are received for distribution must be distributed to those to whom they belong as soon as practicable and without unnecessary delay. The funds which are received for investment must be invested within a reasonable time. The investment of them cannot be delayed unnecessarily.

The place where the trust funds are kept while awaiting investment is of considerable importance. The funds must be kept in safe custody. The custodian may be the trustee bank. But the trustee bank may not use the trust funds in its general banking business unless there is first set aside in the trust department, to protect those funds, an equivalent in bonds of the United States or other securities which have been approved by the Federal Re-

⁶⁴ Federal Reserve Act, *supra* note 2, § 11 (k), par. 3.

⁶⁵ Reg. 1928F, § vii.

serve Board.⁶⁶ The Federal Reserve Board has provided: (1) that the trust funds, held for distribution or investment, can be deposited in the commercial or savings departments of the trustee bank to the credit of the trust department; and (2) the bank must deliver to the trust department, as collateral security:

a. Bonds, notes or other certificates of the United States; or

b. Readily marketable securities. These securities must be of the classes in which the state law of the state within which the national bank is located permits trust companies and state banks having trust powers to invest trust funds; or

c. "Investment securities" as defined by the Comptroller of the Currency. The latter has ruled that investment securities must be marketable securities. And by "marketable" he means that "the security in question has such a market as to render sales at intrinsic values readily possible".⁶⁷

The securities which the bank deposits with the trust department as collateral securities must belong to the bank. They must be at all times equal in market value to the amount of trust funds deposited with the commercial or savings departments of the bank by the trust department.⁶⁸

The trust department of a national bank administers two classes of trusts: (1) private trusts; and (2) court trusts. The investment of both types of trust funds is carefully prescribed by the Federal Reserve Board.

Private Trusts

A private trust is created, usually, by a will, deed, or trust agreement. The funds received under the trust instrument must be invested as soon as is practicable. The investments must be made in strict conformity to the terms of the trust instrument.

⁶⁶ Federal Reserve Act, *supra* note 2, § 11 (k), par. 4.

⁶⁷ Reg. 1928F, § viii; DIGEST OF RULINGS (Fed. Res. Board, 1928) 545. A receipt covering U. S. Liberty Bonds issued by a Federal Reserve Bank and payable on demand to the trust department of a national bank is good collateral security. BULLETIN FEDERAL RESERVE BANK (1921) 545. But bills receivable, loans, or other such paper which the Federal Reserve Bank may discount are not "readily marketable securities." BULLETIN FEDERAL RESERVE BOARD (1920) 380. A deposit of securities with state banking authorities is not a deposit in the trust department of the trustee national bank. *Ibid.* 699.

⁶⁸ Reg. 1928F, § viii.

1. The settlor may indicate specifically the character and type of the investments to be made. He may prescribe the exact nature of the investment. He may forbid investing in designated classes of securities. In such a situation the national bank has no discretion whatever. It must follow the exact instructions given.

2. The trust instrument may contain no instructions whatever as to the nature of the investments to be made. In that situation the investments made are within the discretion of the officers and board of directors of the national bank. But they are governed in their choice by the law of the state within which the national bank is located. They may invest the trust funds in those securities in which the state trust companies and other corporations exercising fiduciary powers within the state are permitted to invest their trust funds. But no other investments may be made.

3. The trust instrument may give the trustee national bank authority to make such investments as the trustee may deem wise and proper. In this situation the board of directors or the investment committee of the national bank may make such investment as their wisdom may dictate. Every national bank or trust company tries to have incorporated within the trust instrument general authority to make such investments as it wishes. This is of considerable advantage to both the trustee and the *cestuis que trustent*. It enables the trustee bank to use its own judgment as to the type of investments to be made. And it gives the *cestuis* the continued benefit of the best judgment of those who are in intimate touch with the financial situation from day to day. In this connection one thing should be noted. Most of the large national banks are affiliated with, or own, investment securities companies.⁶⁹ They are in a position to make investments of trust funds to the great advantage of the beneficiaries of the trusts. But, unless they are given special and specific authority to deal with the investment securities company which they own, or with which they are affiliated, they cannot buy from or sell to that company. This is because of the general rule of the law of trusts

⁶⁹ The National City Bank of New York, for example, owns the National City Company, which is its organ for marketing investment securities.

that the trustee cannot profit, directly or indirectly, to the slightest extent, by reason of the investments of the trust funds which he may make. From the practical standpoint it is wise for the settlor to include in the trust instrument a special provision giving the trustee national bank power to invest the trust funds in such securities as are bought and sold by the investment securities company which is owned by or affiliated with the trustee national bank.

Court Trusts

Trust funds belonging to court trusts are subject to the supervision and control of the court which appoints the trustee. The court may give the trustee specific or general instructions in the matter of investments.

1. If the court gives specific instructions as to the character and type of investments to be made, the national bank must follow those instructions exactly. A copy of every instruction must be filed and preserved in the records of the trust department.⁷⁰

2. If the court gives the trustee national bank general authority to make such investments of trust funds as it may deem proper and wise, the trustee may make such investments as are permitted to trust companies and other fiduciaries by the law of the state in which the national bank is located.⁷¹

3. The court may fail to give either specific or general instructions to the trustee national bank as to investments to be made. In that case the trustee may make such investments as are permitted by the law of the state within which it is located.⁷²

All trust funds must be carefully guarded. It is for this reason that corporations acting in any fiduciary capacity are required by state laws to deposit securities with state authorities to safeguard private and court trusts. In this regard trustee national banks are subject to the laws of the state in which they are located. They must make such deposits as are required of state banks or other corporations acting in fiduciary capacities.

⁷⁰ Reg. 1928F, § ix (b).

⁷¹ *Ibid.*

⁷² *Ibid.*

The deposits must be made with the state authorities. It may happen that the state authorities will refuse to accept such securities. In that event the securities may be deposited with the federal reserve agent of the district within which the national bank is located. Securities deposited with the federal reserve agent must be held so as to protect private and court trusts in accordance with the provisions of the state law.⁷³

In this connection an interesting question presents itself. Suppose that a state law provides that all corporations desiring to exercise trust powers within its territory must deposit securities or cash equal in amount to fifty per cent of its capital. Would the very large national banks with capital running up into the millions of dollars be compelled to deposit fifty per cent of their capital amounts before they would be permitted to do a trust business within that state? There seems to be no case or Federal Reserve Board regulation which deals with this situation. Yet one of the very largest national banks in the country has declined to accept a trust because the state where it would have to be administered has just such a requirement as is above indicated. It is submitted that such a requirement by the state law is unreasonable. It imposes, for all practical purposes, a prohibition upon a large national bank which is not imposed upon smaller national or state banks. In effect it is an interference with the operation of the trust business of the large national bank. It is practically unwise, and also impossible from the standpoint of sound banking principles, to deposit such a huge sum of money in any one state. It cannot have been the intention of Congress or the Federal Reserve Board to enact legislation which practically forbids a national bank from carrying on a trust business in any state having such a law. If the state law called for deposits of securities or cash reasonably necessary to safeguard the trust funds created or administered within that state, there could be no objection. But any law which practically discriminates against a large national bank and in favor of smaller state banks or other state fiduciary corporations is, it would seem, without force and effect. It may with legal safety be ignored.

⁷³ *Ibid.* § vi.

The income from trust funds is, of course, protected as well as the trust funds themselves. The income must be paid promptly when due to the beneficiaries. But before payment is made the trustee national bank is entitled to deduct for its services as trustee proper compensation. The fees of a trustee national bank are determined in four ways.

1. The state law may designate the fees which the trustee national bank may receive for its services in its varying fiduciary capacities.

2. The court which appointed the national bank as a fiduciary may provide by court order what the compensation of the fiduciary is to be.

3. The trust instrument itself may stipulate what the fees or other compensation of the fiduciary national bank shall be.

4. If there is no state law regulating the matter, and no provision has been made by court order or in the trust instrument itself, the trustee national bank is permitted to deduct not more than a reasonable fee for its services.⁷⁴

IV. EXTINCTION OF THE TRUST POWERS OF A NATIONAL BANK

There seems to be no express provision in the banking laws which permits the Federal Reserve Board to withdraw the trust powers which it has conferred upon a national bank. But it cannot be doubted that a failure on the part of the national bank to function properly in its trust department will be sufficient ground for invoking the general authority of the Federal Reserve Board to cancel, through proper court proceedings, all the powers which a national bank has.⁷⁵ In this way the trust powers may be withdrawn from the national bank. But, one ventures to believe, the Federal Reserve Board should be given the authority to exercise its discretion in the withdrawal of one or all of the trust powers conferred by it upon a national bank, without being compelled to dissolve that bank. This authority should be in addition to, and not in exclusion of, the power to dissolve the bank. There is very

⁷⁴ *Ibid.* § x.

⁷⁵ R. S. § 5239, 12 U. S. C. § 93 (1926). This section modifies 38 STAT. 252 (1913).

little likelihood that the Federal Reserve Board would be arbitrary and capricious in its withdrawal of trust powers. If a fear of summary action exists, provisions could be made for a fair hearing of the bank officials. And an appeal would always be possible to the federal courts to prevent any injustice being done to the national bank.

There are, however, some provisions in the regulations of the Federal Reserve Board dealing with the closing out of trusts when the trustee bank becomes insolvent or is placed in voluntary liquidation.

Insolvency

When a national bank becomes insolvent the Comptroller of the Currency appoints a receiver for that bank. It is the duty of the receiver to terminate, as soon as practicable, the trusts which the trustee bank may be operating. He does this under instructions issued to him either by the Comptroller of the Currency, or by courts which may have proper jurisdiction over the several trusts. Such trusts or estates which can be closed out are to be disposed of in that manner promptly. Those trusts and estates which cannot be closed quite promptly must be transferred through appropriate legal proceedings to substitute fiduciaries.⁷⁶

Voluntary Liquidation

When a trustee national bank is placed in voluntary liquidation its receiver must wind up its trust business as soon as practicable. Four situations usually exist.

1. Voluntary trusts which can be cancelled must be cancelled just as soon as possible. All assets and documents connected with the trusts must be turned over to their rightful owners.
2. Court trusts and estates being handled under the jurisdiction of some court must be closed out or disposed of as soon as possible. The orders and instructions of the courts which created the trusts and estates control the disposition of them.
3. All trusts which are not voluntary or court trusts and which can be closed out must be closed as soon as possible. The

⁷⁶ Reg. 1928F, § xiii (a).

trustee bank must make a final accounting to those who are legally entitled to receive that accounting.

4. If there are any trusts or estates which cannot be promptly closed out they must be transferred to substitute trustees or fiduciaries.⁷⁷

The liquidation of the trust department must take place "in accordance with the laws of the State in which" the trustee bank "is located".⁷⁸ It is apparent that the insistence by the Federal Reserve Board that liquidation of the trust business must be in accordance with the state law of the state where the national bank is located creates many difficulties of interpretation and application. Many problems involving the law of "conflict of laws" are presented. In the absence of any decided cases and of any rulings by the Federal Reserve Board in explanation of the foregoing regulation, no statement of law which may help to resolve those difficulties can be made.

⁷⁷ *Ibid.* § xiii (b) 4.

⁷⁸ *Ibid.* § xiii.