INTERPRETIVE LETTER 95-9 (SEPTEMBER 27, 1995)

A corporate fiduciary may not deposit fiduciary account securities with a broker pursuant to the Securities in Fiduciary Accounts Act unless that broker is organized and qualified to accept and execute trusts or the trust instrument directs such a deposit.

This letter is in response to your request for the Illinois Commissioner of Banks and Trust Companies ("Commissioner") to provide written clarification on an issue involving the Securities in Fiduciary Accounts Act ("Act"), 760 ILCS 75 (1994). Specifically, you asked whether a corporate fiduciary may deposit securities with a securities broker pursuant to Section 2(b) of the Act. It is the Commissioner's position that an Illinois corporate fiduciary may not deposit securities with a securities broker unless that broker is authorized to accept and execute trusts or the trust instrument specifically allows for such a deposit.

The Commissioner has criticized the Bank for using brokerage firms to retain securities held in fiduciary accounts. *, stated in correspondence to the Commissioner that he believed a brokerage firm met the definition of a "clearing corporation" under the Act and therefore, the Bank was not in violation of the Act by depositing fiduciary account securities with a broker.

Section 2 provides:

> In addition to all other powers granted corporations authorized to accept and execute trusts in Illinois, such a corporation, when acting as a fiduciary or co-
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> fiduciary, may, unless otherwise provided by the agreement, will, deed, court order or other instrument:
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> > (a) Cause securities to be registered in the name of a nominee..., or

(b) Deposit or arrange for the deposit of securities with a clearing corporation, a Federal Reserve Bank or another fiduciary.

The first issue that must be addressed is if a corporate fiduciary is authorized to hold securities as set out in the Act or is it required that they do so. The Act is not mandatory, but once a corporate fiduciary exercises its authority under the Act, it is bound by the Act=s limitations. The Act was effective on October 1, 1972, and was adopted in response to concerns over the management of physical securities. According to the legislative history of the Act, its purpose is to permit corporate fiduciaries Ato hold shares of the same issuer in bulk@ and to permit those corporate fiduciaries to deposit securities with a

Federal Reserve Bank, clearing corporation or another fiduciary. See General Assembly, Transcription Debates, Senate Bill 1459, June 2, 1972. Prior to the adoption of the Act, a fiduciary could not hold a single certificate representing all of the shares of a single issuer owned by a number of trust accounts. Instead, separate certificates were required to be held. In addition, shares could not be deposited with a clearing corporation, Federal Reserve Bank or another fiduciary in order to simplify the transfer of the share ownership. Each separate certificate was to be transmitted for transfer. The Act was intended to eliminate much of the paper normally associated with the various shares and also to simplify and facilitate the purchase and sale of securities held in a fiduciary capacity. While most corporate fiduciaries follow these procedures, nothing in the Act mandates that shares be held in nominee name or deposited with a third party depository. However, since no other authority exists for such a holding or deposit, a fiduciary is bound by the Act=s provisions if it wishes to use a third party depository.

The second issue is whether a corporate fiduciary may deposit securities with a securities broker or through a Apiggy-back@ relationship with a broker and another fiduciary or clearing corporation. Nothing in the legislative history indicates that the intent was to authorize deposits with brokers or a Apiggy-back@ relationship with the broker and the ultimate depository.

Furthermore, Section 3 of the Act, indicates that securities may only be deposited with another fiduciary, a clearing corporation or Federal Reserve Bank. Section 3 provides:

> The fiduciary shall be liable for the acts of its nominee or the nominee of the clearing corporation, Federal Reserve Bank or other fiduciary, as the case may be, with respect to any security so registered or deposited and shall be liable to the fiduciary account or accounts for its acts and acts of the clearing corporation, Federal Reserve Bank or other fiduciary with respect to the holding of securities in bulk. The records of said fiduciary shall at all times show the ownership of the security by each of the fiduciary accounts and the securities, unless on deposit as authorized by this Act, shall be in the possession and control of said fiduciary in its various fiduciary capacities, and be kept separate and apart from assets which are the individual property of said fiduciary.

The securities of the depositing fiduciary must always be in the possession and control of the fiduciary unless on deposit. When securities are deposited with a clearing corporation, Federal Reserve Bank or another fiduciary, the same fiduciary relationship as to possession and control exist. However, a different relationship exists between a broker and a fiduciary. A broker contract generally provides that the broker will deliver the securities on demand, but the broker does not agree to maintain possession and control. A broker is not a fiduciary, therefore the chain of fiduciary relationships is disrupted when securities are deposited with brokers that lack trust powers.

The Act allows corporate fiduciaries to deposit securities for safekeeping with the above entities and for those entities to hold securities on behalf of the corporate fiduciary. A

Afiduciary@ is defined in Section 1(a) of the Act, as a corporate fiduciary or foreign fiduciary holding a valid certificate of authority from the Commissioner=s Office authorizing it to act in Illinois. A "clearing corporation" is defined in Section 1(c) of the Act as "a corporation as defined in Article 8 of the Uniform Commercial Code **which is authorized to accept and execute trusts"** (emphasis added). Therefore, only a clearing corporation, as defined in the Uniform Commercial Code, that is also authorized to accept and execute trusts, qualifies under Section 2(b) of the Act.

The legislative debates on this issue demonstrate the intent of the Illinois legislature when the Act was enacted. It is clear from those transcripts that a trustee could only deposit securities with a clearing corporation that is also a fiduciary. The Senate sponsor of the legislation that allowed such a deposit with a third party explained on the second reading of the bill:

> [Senate Bill 1459] concerns itself with clearing corporations. The trustee may deposit securities only with the clearing corporation which has been organized in Illinois as a trust company, so that it will be subject to visitation and examination by the commissioner of banks of the State of Illinois. General Assembly, Transcription Debates, June 2, 1972 (statement of Senator Rock).

While the above language would seem to limit deposits of securities to deposits with a clearing corporation that is organized as an Illinois trust company, the plain language of the Act allows for such a deposit with an entity organized to accept and execute trusts, regardless of its state of organization. Therefore, the practice of depositing securities with the Depository Trust Company (ADTC@) remains appropriate. The DTC is a cooperative owned by the financial services industry which serves as a national clearinghouse for the settlement of trades in corporate and municipal securities.

It is the position of the Commissioner=s Office that the terms of the Act are not mandatory, but once a corporate fiduciary chooses to avail itself of the authority in the Act, it is bound by the Act=s limitations. Therefore, a corporate fiduciary may not deposit fiduciary account securities with a broker pursuant to the Act unless that broker is organized to accept and execute trusts or the trust instrument directs such a deposit. Any securities so held by a broker should be transferred to an appropriate depository institution within a reasonable time period from the date of this letter.