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House Bill 5833 (Substitute H-1 as passed by the House)

Sponsor: Representative Matt Milosch

House Committee: Commerce

Senate Committee: Banking and Financial Institutions

Date Completed: 12-2-04

## **CONTENT**

**The bill would amend Public Act 174 of 1941, which authorizes financial institutions to establish and maintain "common trust funds" for the collective investment of money contributed by a financial institution in its capacity as a fiduciary, to allow financial institutions also to establish and invest in "collective investment funds", which would consist of assets of retirement, profit-sharing, or other tax-exempt employee benefit trusts. The bill would do all of the following:**

- Regulate the investment of common trust funds and collective investment funds.**
- Prohibit a financial institution administering a fund from having an interest in it, other than as a fiduciary.**
- Require each common trust fund and collective investment fund to have a fund plan, and specify minimum requirements for fund plans.**
- Require a financial institution administering a fund to have it audited annually and to prepare a financial report based on the audit.**
- Require a financial institution administering a fund to determine the value of its assets periodically.**
- Regulate distribution from common trust funds and collective investment funds.**
- Allow a financial institution administering a fund to charge a reasonable management fee and reasonable expenses.**
- Specify additional types of investments that a financial institution could make with assets it held as a fiduciary.**

**The bill also would rename Public Act 174 the "Collective Investment Funds Act".**

"Common trust fund" currently means a fund maintained by a financial institution, exclusively for the collective investment and reinvestment of money contributed to the fund by the financial institution in its capacity as a fiduciary or cofiduciary and established, maintained, and administered pursuant to the Act. Two or more financial institutions must be treated as one with respect to a fund of which any one of the institutions is trustee or two or more of the institutions are cotrustees. Under the bill, "common trust fund" instead would mean a fund maintained by a financial institution or one or more affiliated financial institutions exclusively for the collective investment and reinvestment of money contributed to the fund by the financial institution or the affiliated financial institutions in its capacity as a fiduciary or cofiduciary.

"Collective investment fund" would mean a fund maintained by a financial institution or by one or more affiliated financial institutions that consisted solely of assets of retirement, pension, profit sharing, stock bonus, or other trusts exempt from Federal income tax.

Under the bill, "fund" would mean either a common trust fund or a collective investment fund.

"Fiduciary" currently means a financial institution or person acting in the capacity of executor, administrator, administrator with the will annexed, administrator de bonis non guardian, testamentary trustee, trustee appointed by any court, and trustee under a written agreement, declaration, or instrument of trust, either solely or together with others. Under the bill, "fiduciary" instead would mean a financial institution or other person acting in the capacity of guardian, conservator, personal representative, or trustee, either solely or together with others, or custodian under any state's Uniform Gift or Transfer to Minors Act.

### Investment of Funds

Under the Act, a financial institution, in its capacity as a fiduciary or cofiduciary, may invest funds that it lawfully holds for investment in that capacity in interests or participations in one or more common trust funds, if the investment is not prohibited by the instrument, judgment, decree, or order creating the fiduciary relationship. The bill also would allow a financial institution to invest assets of retirement, pension, profit sharing, stock bonus, or other employee benefit trusts exempt from Federal income tax that the financial institution held in any capacity, including agent, in a collective investment fund.

Presently, the funds and assets of a common trust fund may be invested and reinvested in investments or items in which a person acting in a trust or fiduciary capacity, and who is not limited or restricted by investment specification or limitations, may invest trust funds under Michigan law. The bill would delete that provision. The bill specifies that a financial institution could invest and reinvest the assets of a fund in accordance with the plan for that fund.

Under the bill, a financial institution administering a fund could not have an interest in that fund other than in its fiduciary capacity. If, because of a creditor relationship or otherwise, a financial institution acquired an interest in a participating account, the institution would have to withdraw the participating account from the fund on the next withdrawal date. A financial institution, however, could invest assets that it held as fiduciary for its own employees in a fund.

A financial institution administering a common trust fund or a collective investment fund could not make any loan secured by a participant's interest in the fund. An unsecured advance to a fiduciary account participating in the fund until the time of the next valuation date would not constitute the acquisition of an interest in a participating account by the financial institution.

A financial institution administering a fund could purchase for its own account any defaulted investment held by the fund rather than segregating the investment, if the financial institution considered the cost of segregating the investment excessive in light of its market value. If a financial institution elected to purchase a defaulted investment, it would have to purchase it for its market value or the sum of cost and accrued unpaid interest on the defaulted investment, whichever was greater.

### Fund Plans

The Act requires that each common trust fund be established and maintained in accordance with a written plan approved by resolution of the financial institution's board of directors. Under the bill, either a common trust fund or a collective investment fund would have to be established and maintained in accordance with a written plan approved by resolution of the institution's board of directors or a committee authorized by the board.

The bill would delete the current requirements for a common trust fund plan and require, instead, that a fund plan contain full and detailed provisions as to the manner in which the financial institution would operate the fund, including all of the following provisions:

- The investment powers and policies with respect to the fund.
- The allocation of income, profits, and losses.
- The fees and expenses that the financial institution would charge to the fund and to participating accounts.
- The terms and conditions governing the admission and withdrawal of participating accounts.
- How participating accounts would be audited.
- The basis and method of valuing assets in the fund.
- The expected frequency of income distribution from the fund to participating accounts.
- The minimum frequency of valuation of fund assets.
- The period of time following a valuation date in which a valuation of fund assets would have to be made.
- The bases upon which the financial institution could terminate the funds.
- Any other matters necessary to define clearly the right of participating accounts.

A financial institution would have to make a copy of a written plan available at its principal office for inspection during all regular business hours and provide a copy to any person who requested it.

#### Audit & Report

At least once during each 12-month period, a financial institution administering a fund would have to arrange for an audit of the fund by auditors responsible only to the financial institution's board of directors, as well as prepare a financial report of the fund based on the audit. The report would have to disclose the fund's fees and expenses, a list of investments in the fund, the cost and current market value of each investment, and a statement covering the period after the previous report that showed all of the following, organized by type of investment:

- A summary of purchases, including costs.
- A summary of sales, including profit or loss and any other investment changes.
- Income to and disbursements from the fund.
- A description of any investment in default.

A financial institution administering a fund would have to provide a copy of the report, or a notice that a copy of the report was available upon request without charge, to each person who ordinarily would receive a regular periodic accounting with respect to each participating account. The financial institution could provide a copy of the report to prospective customers and could provide a copy, upon request, to any person for a reasonable charge.

#### Valuation & Distribution

Under the Act, at least once during each three-month period, a financial institution administering a common trust fund must determine the value of the assets in the fund. No participation may be admitted to or withdrawn from the common trust fund except on the basis of the valuation and on the date of the determination of the valuation or, if permitted by the plan, within two business days after that date. When participation is withdrawn from a common trust fund, distributions may be in cash or ratably in kind, or partly in each. The bill would delete these provisions.

Under the bill, a financial institution administering a fund that was not invested primarily in real estate or other assets not readily marketable would have to determine the value of the fund's assets at least every three months. A financial institution administering a fund that was invested primarily in real estate or other assets that were not readily marketable would have to determine the value of the fund's assets at least once a year. A financial institution administering a fund could admit an account to or withdraw an account from the fund only on the basis of such a quarterly or yearly valuation.

A financial institution administering a fund could admit an account to or withdraw an account from the fund only if it had approved a notice of taking that action on or before the valuation date. A request or notice could not be canceled or countermanded after the valuation date.

A financial institution administering a fund would have to make distributions to accounts withdrawing from the fund in cash, ratably in kind, in a combination of cash and ratably in kind, or in any other manner consistent with applicable law in the state in which the financial institution maintained the fund. If an investment were withdrawn in kind from a fund for the benefit of all participants in the fund at the time of the withdrawal, but the investment were not distributed ratably in kind, the financial institution would have to segregate and administer the investment for the benefit ratably of all participants in the fund at the time of withdrawal.

### Administration Fee

The bill would allow a financial institution administering a fund to charge a reasonable management fee that was not more than the value of legitimate services of tangible benefit to the participating accounts that would not have been provided to the accounts if they were not invested in the fund. A financial institution administering a fund also could charge reasonable expenses incurred in operating the fund.

### Other Investments

The bill would delete a provision that nothing in the Act prohibits a financial institution from establishing, maintaining, and administering one or more common trust funds differing from the requirements of the Act, in which only investments or participations are made by the financial institution in accordance with specific contract authority.

The bill instead lists types of investments (in addition to a fund) in which a financial institution could invest assets it held as fiduciary, to the extent not prohibited by applicable law. For purposes of these other investments, a financial would act as fiduciary if it acted as any of the following:

- A trustee, personal representative, executor, administrator, registrar of stocks and bonds, transfer agent, guardian, assignee, receiver, or custodian under any state's Uniform Gifts or Transfers to Minors Act.
- An investment adviser, if the financial institution received a fee for its investment advice.
- In any capacity in which the financial institution possessed investment discretion on behalf of another.
- In any similar capacity that a Federal banking agency having authority over the financial institution authorized from time to time.

MCL 555.101 et al.

Legislative Analyst: Patrick Affholter

### **FISCAL IMPACT**

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: Maria Tyszkiewicz

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.