



The Rise of the American Statutory Business Trust

SCIBL:
The Regulation of Wealth Management
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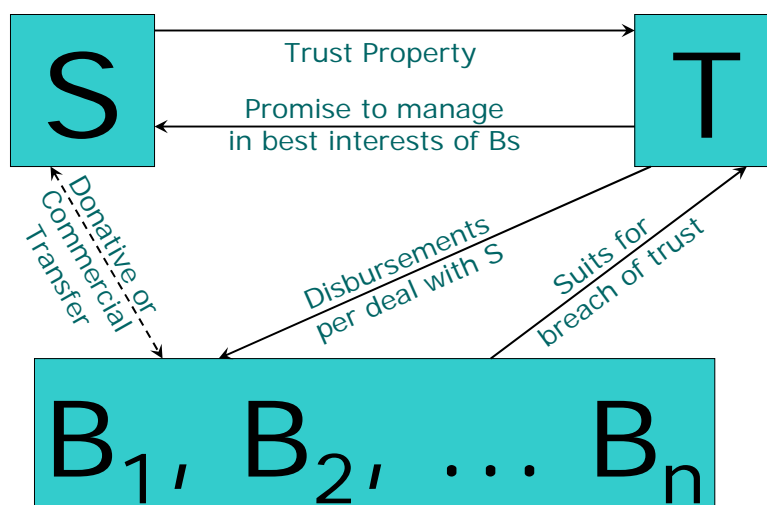
The Statutory Business Trust

- Since 1988, 8 DE-based modern acts
 - Pending in NY
 - Drafting in CA
 - Uniform Statutory Trust Entity Act (in draft)
- 3/4 mutual funds are business trusts
 - \$10 trillion industry
 - more than 1/3 American households has an interest in a modern business trust
- Common in securitization
 - estimates range \$2 to \$5 trillion
- Yet, no systematic scholarly inquiry

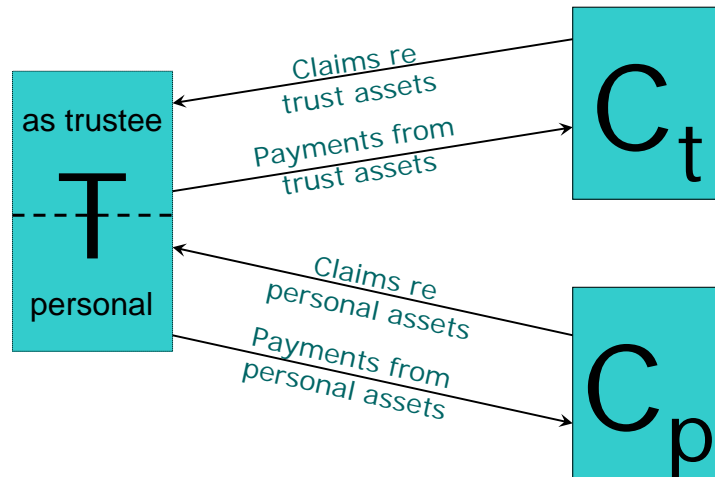
First-Cut Study: Six Foci

- Rise/fall common law business trust
- The business trust statutes: A taxonomy
- Jurisdictional (interstate) competition
- SBTs in practice (i.e., inter-entity competition)
- Why a niche entity?
- The USTEA and its potential impact

Figure 1a:
The Trust as Organizational Form (Internal)



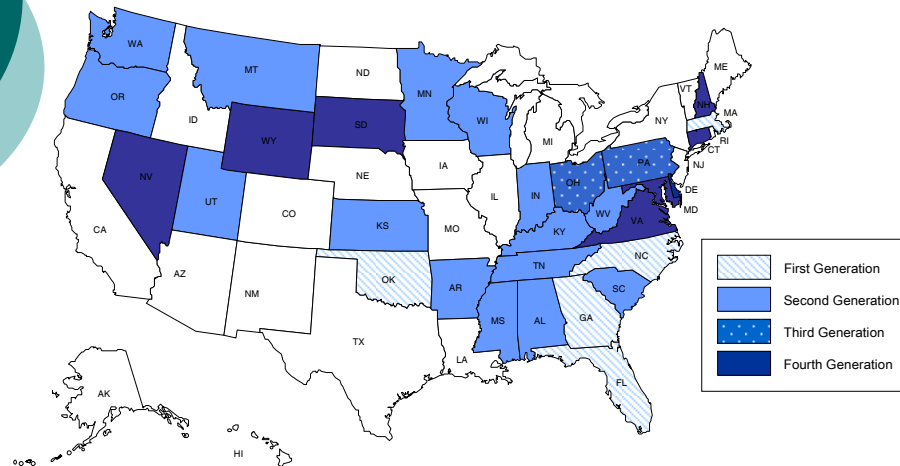
**Figure 1b:
The Trust as Organizational Form (External)**



The Rise and Fall of the Common Law Business Trust

- Late 1800s, early 1900s
 - Corporations are heavily regulated
 - Trusts arise from private agreement
- Rise: Avoiding corporate regulation
 - Real estate, stock, capitalization
 - Hence *antitrust* law, "Massachusetts trust"
- Fall: Uncertainty and judicial hostility
 - public policy/corporate law
 - limited liability
 - entity shielding
- Permissive corporate law

Figure 2: Business Trust Legislation



The Business Trust Statutes

- First generation (5) (early 1900s)
- Second generation (15) (1960s)
- Third generation (2) (1980 - 1988)
- Fourth generation (8) (since 1988)
 - Delaware [Statutory] Trust Act (1988)
 - Seven Delaware mimics (plus USTEA)
 - Perfects entitization of the trust
 - Few defaults, fewer mandatory rules
 - Freedom of contract (eliminate fido duties?)
 - Trust law fills gaps: a statutory trust entity

Jurisdictional Competition

- Measurement: Formation Data

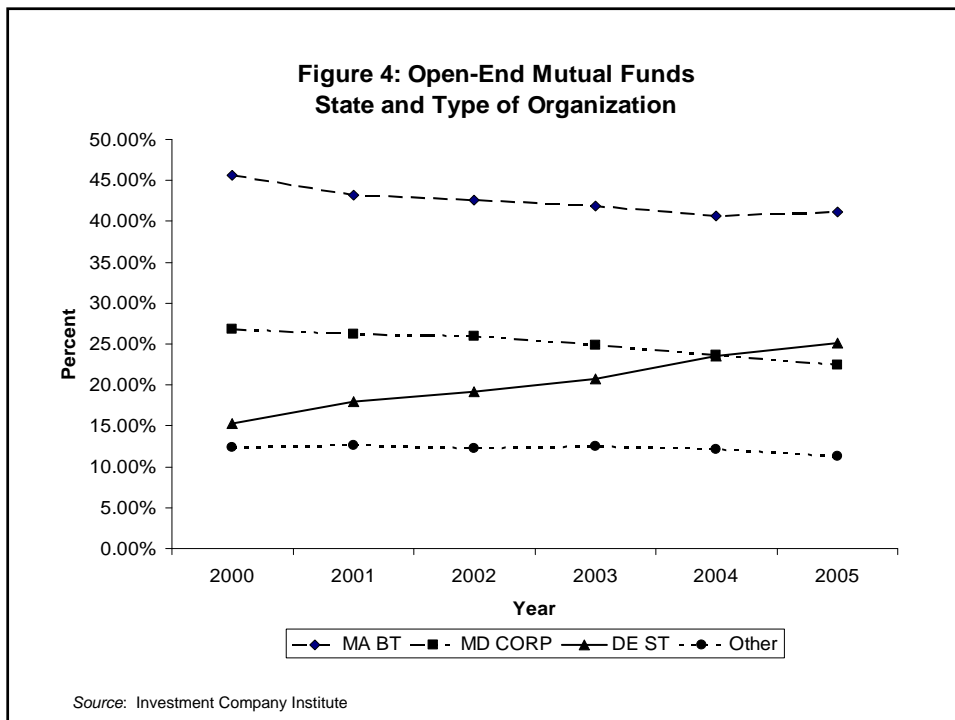
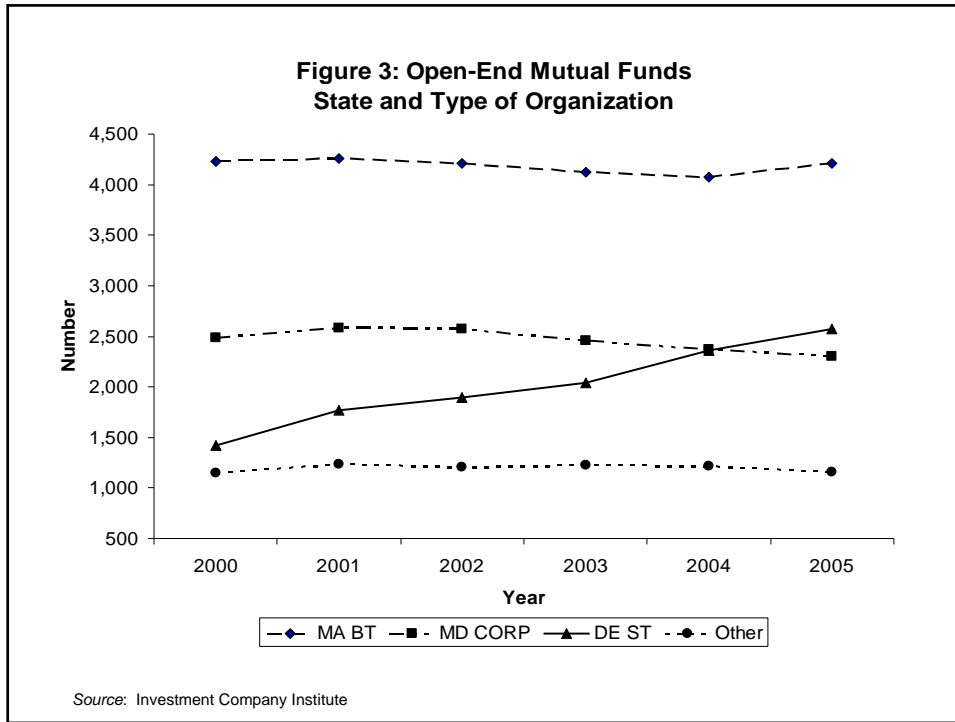
	2003	2004	2005	2006
CT	1,331	1,430	1,555	1,624
		99	100	159
DE	9,903	11,535	14,164	17,208
	1,722	1,900	3,200	3,904
MA			10,531	10,370
	153	101	104	88

- Mechanisms: Interest Groups or Taxes
- Welfare: Race to Top or Bottom

SBTs in Practice: Interentity Competition

- Not REITs
- Mutual Funds
 - Flexibility (shares, meetings), 1940 Act Provisions
 - ICI Data

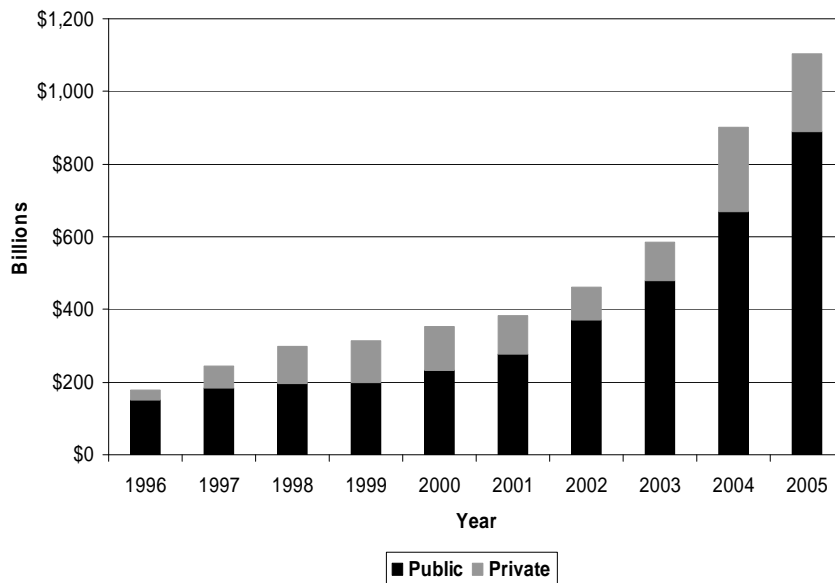




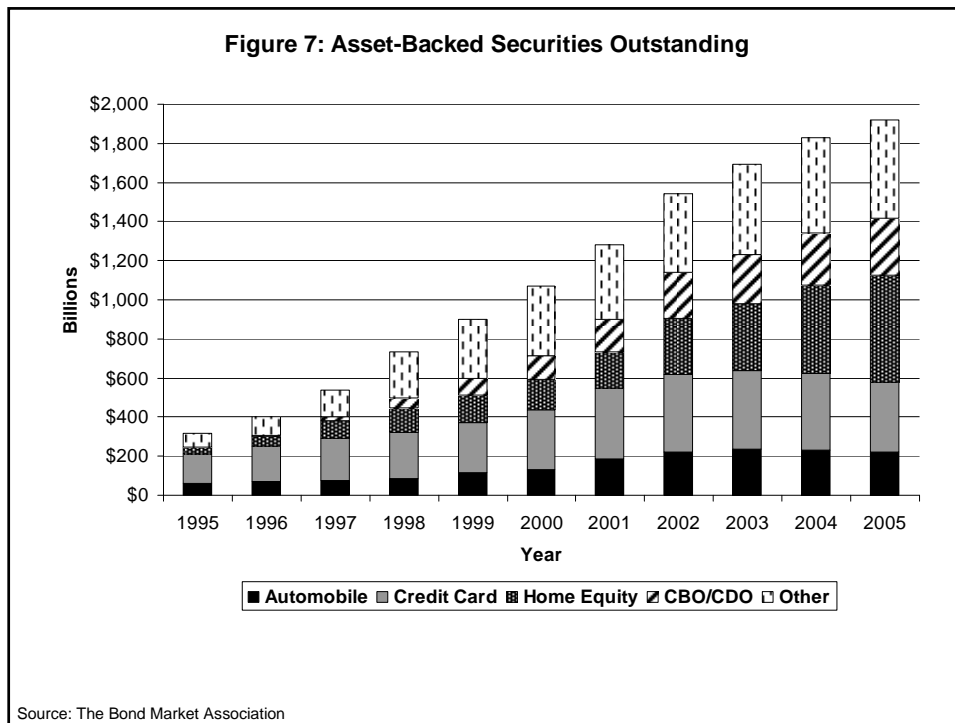
SBTs in Practice: Interentity Competition

- Not REITs
- Mutual Funds
 - Flexibility (shares, meetings), 1940 Act Provisions
 - ICI Data
- Structured Finance
 - Bankruptcy remote
 - Federal Reserve and BMA volume data
- Miscellaneous
 - IRC 1031 exchanges
- Not REITs
- Summary: Opportunistic niche entity
 - Theory fits lack of decisions
 - Total Volume Estimate

Figure 6: Asset-Backed Securities Issuance



Source: The Bond Market Association



SBTs in Practice: Interentity Competition

- Not REITs
- Mutual Funds
 - Flexibility (shares, meetings), 1940 Act Provisions
 - ICI Data
- Structured Finance
 - Bankruptcy remote
 - Federal Reserve and BMA volume data
- Miscellaneous
 - IRC 1031 exchanges
- Summary: Regulatory Arbitrage
 - Theory fits reality of
 - lack of decisions, and
 - many SEC no-action letters

Volume in Dollars: Rough Calculation

- $\frac{3}{4}$ of \$10 trillion mutual fund assets
 - = \$7.5 trillion
- $\frac{1}{2}$ of \$6 trillion securitization assets
 - = \$3 trillion
- So, SBTs hold in the neighborhood of \$10.5 trillion!

Why a Niche Entity?

- "In theory, any entity that can be formed as a business corporation, an LLC, an LLP, or an LLLP could be formed instead as a statutory business trust."
 - Hansmann, Kraakman, and Squire (2005)
- Potential Explanations
 - Continuing legal uncertainty
 - Transaction costs: mismatch in default rules
 - Path dependency, network effects, status quo bias
 - Public provision of the corporate contract
 - Agency costs in legal services
- Welfare consequences?



Uniform Statutory Trust Entity Act

- Fourth-generation, modeled on DE
 - Express override of mismatch trust defaults
 - Relation to common law trust
 - Exclusion of donative purpose
 - Schedule of mandatory rules
 - “manifestly unreasonable” limit
- Perfects entitization of the trust
 - Addresses uncertainty of old cases
 - Entity shielding
- Economics of uniform laws
 - If widely adopted, natural experiment on prior slide’s hypotheses