

1980 WL 120959 (S.C.A.G.)

Office of the Attorney General

State of South Carolina

November 5, 1980

***1 Re: Money Market Funds**

The Honorable Arnold S. Goodstein
P. O. Box 7505
C & S Financial Center
North Charleston, South Carolina 29406

Dear Senator Goodstein:

You have requested an opinion from this office with regard to whether money market funds, which offer checking account privileges to investors, are in violation of the South Carolina banking laws. Because of the number of different funds available, each with its own particular characteristics, it was necessary to examine one such fund in detail in order to offer an opinion with any degree of specificity. I have selected the Merrill Lynch Ready Assets Trust (MLRAT) as the subject for my opinion. Therefore, this opinion may not be applicable to other funds which might vary significantly from MLRAT. I have spent a great deal of time gathering and studying information about MLRAT. In this regard, I reviewed the MLRAT prospectus, as well as various opinions rendered by the United States Justice Department, the Attorney General of Alaska, the Attorney General of Louisiana, and statements given to the United States Senate's Subcommittee on Financial Institutions by representatives of the Securities and Exchange Commission and the Federal Reserve System.

BACKGROUND

Money market funds are usually organized as corporations or business trusts by individuals associated with an existing company engaged in the business of providing investment management services. Capital raised from the sale of shares is invested in a variety of short-term money market instruments and the returns are distributed to the shareholders in the form of dividends. Investment objectives cited in the Merrill Lynch Ready Assets Trust (MLRAT) prospectus are to preserve shareholder capital, to maintain liquidity, and to achieve the highest possible income. According to the prospectus, the advantages of such an investment include reduced risks because of the diversified assets, high liquidity, high potential yield and relief from administrative burdens.

METHOD OF OPERATION OF MERRILL LYNCH READY ASSETS TRUST

A minimum initial purchase of \$5,000.00 is invested by the shareholder. Each subsequent purchase must be in increments of \$1,000.00, and the Trust reserves the right to involuntarily redeem shares if the value of the shareholder's account falls below \$1,000.00. The net asset value of each share is normally constant at \$1.00 per share while any fluctuation in the value of the assets owned by the money market fund is reflected in the number of shares held by a stockholder. The quantity of shares owned by an investor is calculated daily.

Ordinarily the dividends are reinvested daily in the form of additional shares and a monthly statement of these reinvestments is sent to the shareholder. The investor may, however, elect to receive a monthly cash dividend payment. Other shareholder services include an exchange privilege with other Merrill Lynch investment funds, the option of receiving regular monthly or quarterly withdrawal checks and the possibility of making regular additions at a minimum of \$50.00 per month. (In the prospectus it is noted that withdrawals of this type are not dividends, yield, or income but are instead sales of shares which may result in taxable gain or loss.)

*2 The check-writing privilege is described as a form of redemption of shares at net asset value. Shares are redeemed by presenting a check for at least \$500.00 to the transfer agent, the Bank of New York. The bank in turn presents the check to the Trust as authority to redeem a sufficient number of shares in the investor's account to cover the amount of the check. The investor pays no interest penalty and continues to receive dividends on invested shares until the check is presented for payment.

STRUCTURE OF TRUST

The Merrill Lynch Ready Assets Trust is an unincorporated business trust organized under the laws of Massachusetts. MLRAT is described as a no-load, diversified, open-end investment company. An investment company has been defined as a corporation whose business consists of, and is limited to, investing in the securities of other corporations on behalf of its investors or shareholders for the purpose of capital appreciation, income preservation or safety of capital, or for a combination of such purposes. An investment company sells its own securities to the public and then reinvests the proceeds in a portfolio of investment securities which it manages on a continuous and full-time basis. 42 Am.Jur.2d Investment Companies and Advisers, § 1 (1969). An open-end company, commonly called a mutual fund, continuously offers its shares for sale to the public and redeems its own shares, so that an investor purchases shares from and resells them back to the mutual fund, rather than from or to another investor. 42 Am.Jur.2d Investment Companies and Advisers, § 3. The term 'no-load' indicates that there is no brokerage fee for sale of the shares.

OPINION

The South Carolina Code of Laws (1976) contains several general definitions of 'banks' and 'banking institutions': Except when otherwise specifically provided the term 'bank' as used in this Title shall be construed to include cash depositories and all institutions doing any kind of banking business. . . . [Section 34-1-10 of the 1976 Code](#).

The term 'banking institution', as used in this article shall be construed to mean any bank, trust company, bank and trust company, stock savings bank, mutual savings bank or cash depository which is now or may hereafter be organized under the laws of this state. [Section 34-3-610 of the 1976 Code](#).

'Bank', any national banking association or any state bank, savings bank, trust company, and all institutions doing any kind of banking business, whether organized under the laws of this state, the laws of another state, or the laws of the United States, engaged or authorized to engage in the business of banking in this state. Section 34-23-20(a) of the 1976 Code.

There is no specific statutory definition of what constitutes the business of banking. It has been simplistically defined, however, as the receipt of deposits of money, the lending of money, and the issuance of promissory notes. Thus, a bank is a place of business where credits are opened by the deposit or collection of money or currency, subject to be paid or to be remitted upon draft, check or order. 10 Am.Jur.2d, Banks, § 1. The South Carolina courts recognize the accepted principle that the relationship between a general depositor and his bank is that of creditor and debtor. [Singletary & Son, Inc. vs. Lake City State Bank, 243 S.C. 180, 133 S.E.2d 118 \(1963\)](#).

*3 Business trusts are not ordinarily considered to be banking institutions. The general practice nationwide is to require that business trusts comply with state and federal securities regulations. 13 Am.Jur.2d, Business Trusts, §§ 80, 82. Although a business trust has certain features in common with an ordinary trust, a partnership, and a corporation, the general opinion is that the business trust should be regarded as sui generis. 13 Am.Jur.2d, Business Trusts, § 3 (1964). A business trust is said to be essentially a business organization cast in the trust form. [Annot. 88 A.L.R.3d. 704 \(1978\)](#). If there is no statutory definition, the business trust is usually defined as an unincorporated business organization created by an instrument by which property is to be held and managed by trustees for the benefit and profit of such persons as may be or become holders of transferable certificates evidencing the beneficial interests in the trust estate. 13 Am.Jur.2d, Business Trusts, § 1.

Business trusts differ from ordinary trusts in that the primary purpose of the business trust is to conduct a business for profit, while the object of the traditional trust is to hold and conserve particular property. Thus, the Restatement of the Law of Trusts excludes coverage of business trusts, pointing out that the business trust is a special kind of business association and can best be dealt with in connection with other business associations. 13 Am.Jur.2d, Business Trusts, §§ 1, 8. Indeed, the South Carolina Code appears to distinguish between a 'trust company' and a 'business trust.' For example, the Uniform Commercial Code defines 'organization' to include both a 'business trust' and a 'trust.' Section 36-1201(28) of the 1976 Code. Likewise, the South Carolina Bank Holding Company Act appears to distinguish between the two terms in defining the term 'company' to include 'business trust' but defining 'bank' to only include 'trust company' and not a 'business trust.' Therefore, it is my opinion that a 'business trust' is not specifically included in the definition of 'banks' and 'banking institutions' stated previously.

There still remains the question, however, of whether MLRAT would fall under the banking laws of South Carolina because it operates or functions as a bank. The commonly accepted definitions of 'banking' focus on the receipt of deposits as the central factor in determining whether a certain activity constitutes the business of banking. For example, Title 12, Section 36(f) of the U. S. Code defines a branch bank as any place of business where deposits are received, checks paid, or money lent. The receipt of deposits, of course, establishes a fixed liability and a debtor-creditor relationship between the parties. Singletary & Son, Inc. v. Lake City State Bank, *supra*. On the other hand, the test commonly employed to determine if an instrument is a security is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others. 69 Am.Jur.2d, Federal Regulation of Securities, § 69. Our examination of the structure and operation of the MLRAT indicates that shares in the trust are investments rather than deposits. In particular, it is noted that the investment does not create a fixed liability; rather the value of the investment will fluctuate according to market conditions requiring shareholders to participate in the trust's losses as well as its profits. Although there are certain distinctions between a money market fund and the traditional security, they seem to be differences of degree and not of substance. A stock investment is generally more speculative than an investment in a money market fund. The typical open-end investment company distributes net earnings quarterly while the money market fund computes earnings daily and money market funds are distributed at 'no load' without the use of a dealer network. However, the money market fund shareholder does fulfill the traditional role of an investor by 1) electing management; 2) ratifying major management decisions; and 3) sharing in profits and losses resulting from investment activity.

*4 The Opinion of the Attorney General of Louisiana, enclosed with your opinion request, noted the following activities as being similar to the functions of banks:

- 1) the shareholder may withdraw his funds at any time without liquidation penalties;
- 2) the shareholder is not assessed any service charge when opening or closing the account;
- 3) the shareholder receives monthly statements of his account;
- 4) the Trust invests a shareholder's money in government paper, certificates of deposit, banker's acceptances or commercial paper;
- 5) the shareholder can write checks on his account.

In my opinion, the first four activities could not be considered activities peculiar to the banking industry. Since check writing privileges are normally a 'banking' function closer scrutiny of this activity is required. The check-writing privilege is described in the MLRAT prospectus as a method of share redemption. The Louisiana Opinion failed to note that the check is drawn on the Bank of New York which operates as the 'Transfer Agent' for the Trust. The proceeds are payable out of a custody account maintained by the Trust with the Bank of New York. Since the check is not drawn on the Trust itself, it is my opinion that the MLRAT is not engaging in 'banking.' The check-writing privilege is merely one form that a shareholder may use to redeem his investment.

I hope this opinion has been of assistance to you. If you should have any further questions, please do not hesitate to contact me.
Very truly yours,

Richard B. Kale, Jr.
Senior Assistant Attorney General

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