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NOTES

THE TRANSFER AGENT'S RESPONSIBILITY IN
FIDUCIARY SECURITY TRANSFERS

The transfer agent is responsible for the transfer of corporation securities upon the books of the corporation. This agent may be an individual or a department of the corporation itself, but is usually a bank or trust company with a special transfer department and trained staff.

A fiduciary transfer is a transfer other than a normal transfer by an individual in his own name.¹ The most frequently occurring types are:

1. Transfer of a decedent's stock by his executor or administrator. (The stock may be registered in decedent's name or the name of the executor or administrator).
2. Transfer of stock registered in the name of a trustee on the endorsement of the trustee.
3. Transfer of stock in the name of a minor.
4. Transfer of stock registered in the name of a guardian of a minor or incompetent on the endorsement of the guardian.
5. Transfer of stock registered in the name of a corporation on the endorsement of an officer.
6. Transfer of stock registered in the name of a partnership on the endorsement of one of the partners.
7. Transfer of stock registered in the name of a principal on the endorsement of the agent.
8. Transfer of stock on the endorsement of a fiduciary to the individual name of the fiduciary.

"The transfer agent must pass on and satisfy itself as to the validity and propriety of the transfer. He is generally held liable for the improper issue and transfer of certificates both to the corporation and to persons injured."²

This rule of liability was not a part of the law of England. There the rule was that a corporation was not bound to notice trust of its stock and could look solely to the legal estate.³ In the United States, the rule had its origin in *Lowry v. Commercial and Farm-*

1. Christy, *Responsibilities in the Transfer of Stock*, 53 Mich. L. Rev. 701 (1955).

2. 12 Fletcher, *Cyc. Corp.* § 5537.1 (Perm. ed. 1957). There is no liability on the transfer agent to the person injured in the case of a wrongful delay or refusal to transfer. See Fletcher, *op. cit. supra*, § 5525, quoted in *Hulse v. Consolidated Quicksilver Mining Corp.*, 65 Idaho 768, 154 P.2d 149, 154 (1944).

3. *Hartga v. Bank of England*, 3 Ves. Jr. 55, 30 Eng. Rep. 891 (1796).

ers' Bank⁴ and has now become firmly established by subsequent decisions.

Leading authorities have criticized the rule imposing liability for the registration of security transfers in breach of trust.⁵ It is thus in their efforts to avoid liability that transfer agents have been compelled to insist upon a wide variety of documentation⁶ as a prerequisite to registering the transfer of securities held in a fiduciary capacity. Legislative intervention was inevitable in the form of "exoneration statutes." Before examining the various statutes it may be wise to point out two fundamental types of responsibility which are often difficult to distinguish.

The first is the unauthorized and void transfer, commonly referred to as "wrongful." Examples are: a transfer on a forged endorsement, by a corporation officer⁷ or agent⁸ without authority; by a fiduciary not legally appointed or previously removed⁹ and who endorses in the name of a minor, decedent or incompetent and; by a fiduciary without court order where such transfers are void.¹⁰ The various exoneration statutes are not designed to relieve the transfer agent of liability for registering wrongful transfers.

The second type of transfer presents a more difficult problem. It is the transfer by a fiduciary in breach of trust. This type of transfer is not void, but rather voidable at the suit of the beneficiary or successor fiduciary. It is a transfer not in the regular course of administration of the trust or not in accordance with the terms of the trust.¹¹

"No one quarrels much with the requirements imposed by a transfer agent to protect itself against wrongful transfers, such as a signature guarantee, a certified copy of a corporate resolution, evidence of the appointment of the fiduciary, and a court order where

4. 15 Fed. Cas. 1040, No. 8581 (C.C. Md. 1848) where Taney, J. said (at p. 1047) "The corporation is thus made the custodian of the shares of stock, and clothed with power sufficient to protect the rights of everyone interested from unauthorized transfers; it is a trust placed in the hands of the corporation for the protection of individual interests, and like every other trustee, it is bound to execute the trust with proper diligence and care, and is responsible for any injury sustained by negligence or misconduct."

5. See Scott, *Participation in a Breach of Trust*, 34 Harv. L. Rev. 454, 482 (1921); Christy, *supra* note 1, 701.

6. Typical documentation required for a transfer of stock on behalf of a decedent's estate include: (1) the certificate, assignment and signature guarantee (as in a normal Transfer), (2) a court clerk's certificate of appointment of the fiduciary, (3) a certified copy of the will, if any, (4) a court order authorizing sale or distribution (where required by law), (5) inheritance tax waivers from states having contact. Conrad, *A New Deal for Fiduciaries Stock Transfers*, 56 Mich. L. Rev. 943, note 1 (1958).

7. Jennie Clarkson Home v. M. K. & T. Ry. Co., 182 N. Y. 47, 74 N.E. 571 (1905).

8. St. Romes v. Levee Steam Cotton Press Co., 127 U.S. 614 (1888); Quay v. Presidio & F. R. Co., 82 Cal., 22 Pac. 925 (1889).

9. Mobile & O. Ry. Co. v. Humphries, 7 So. 522 (Miss. 1890).

10. Weyer v. Second Nat. Bank, 57 Ind. 198 (1877).

11. Christy, *supra* note 1, at 705.

it is necessary for the transfer. The quarrel comes when the transfer agent asks to look at the will or the trust instrument and then requires an executor to prove that all the debts of the estate have been paid, or that the transfer is by way of sale of the shares, or that the transferee is a legatee; or requires a trustee to prove that he has a power of sale, or that the life tenant is dead, where the transferee is a remainderman, or that the transferee has reached the age when distribution to him is directed by the trust instrument; or requires a guardian to prove that his ward has reached majority, where the transfer is to the ward; or requires any fiduciary to prove that a transfer to his individual name is proper. But, under existing law, the transfer agent must look at such papers and must require such proof. To eliminate this duty of a transfer agent is not unfair to the beneficial owner of the stock. The fiduciary was selected by the person creating the fiduciary relationship, and the transfer agent should not have to be a watchdog to keep him honest."¹²

Section 3 of the Uniform Fiduciaries Act¹³ was intended to expedite transfers "relieving trust estates from delay resulting from the rule imposing a stringent duty of investigation upon corporations registering transfers."¹⁴ Section 3 has been adopted in North Dakota¹⁵ with "nominees of fiduciaries" included within its coverage.

The shortcomings of Section 3 are obvious. It applies only when securities are registered in the name of a fiduciary. This prevents its application in the many cases where securities are registered in the name of the beneficial owner. Perhaps the principal objections are centered around the exceptions, in cases of "bad faith" or "actual knowledge." The problem with the former term (as in most acts utilizing the term) is one of definition, while the latter involves

12. Christy, *supra* note 1, at 705. Ordinary diligence, and not suspicious watchfulness is the measure of duty which a corporation owes to its stockholders" *Peck v. Providence Gas Co.*, 17 R. I. 275, 284, 21 Atl. 543 (1891).

13. Uniform Fiduciaries Act, § 3, 9B ULA "If a fiduciary, in whose name are registered any shares of stock, bonds or other securities of any corporation, public or private, or company or other association, or of any trust, transfers the same, such corporation or company or other association is not bound to inquire whether the fiduciary is committing a breach of his obligation as a fiduciary in making the transfer, or to see to the performance of the fiduciary obligation, and is liable for registering such transfer only where registration of the transfer is made with actual knowledge that the fiduciary is committing a breach of his obligation as a fiduciary in making the transfer, or to see to the performance of the fiduciary obligation, and is liable for registering such transfer only where registration of the transfer is made with actual knowledge that the fiduciary is committing a breach of his obligation as a fiduciary in making the transfer, or with knowledge of such facts that the action in registering the transfer amounts to bad faith."

14. See *Mudge v. Mitchell Hutchins & Co.*, 322 Ill. App. 409, 425, 54 N.E.2d 708, 714 (1944).

15. N.D. Rev. Code, § 10-18021 (Supp. 1957).

the possibility of actual knowledge by a corporate officer or agent who had nothing to do with the transfer.

"Whether or not the Fiduciaries Act relieved transfer agents of liability, it failed to relieve them of the fear of liability, and hence they have continued to require the production of trust instruments before they are willing to register a transfer."¹⁶

Miscellaneous state acts¹⁷ have also been of little success in reducing the amount of documentation required. The success obtained has often not been uniform throughout the particular state.¹⁸

The Uniform Commercial Code, Sections 8-401, 8-402 and 8-403,¹⁹ deal with the responsibilities of a transfer agent in making

16. SCOTT, COMMENT ON THE UNIFORM ACT FOR THE SIMPLIFICATION OF FIDUCIARY SECURITY TRANSFERS. See also the results of a New York survey cited in Conrad, *supra* note 6, at 846.

17. See, e. g., Ohio Rev. Code, § 1339.02, 2109.29 (Page 1954); *id.* § 1701.28 (Supp. 1957); Wis. Stat. Ann. § 108.85 (West 1957); Mass. Laws Ann. c. 203, § 21 (1955).

18. Conrad, *supra* note 6, at 848.

19. U.C.C. § 8-401 (1) Where a security in registered form is presented to the issuer with a request to register transfer, the issuer is under a duty to register the transfer if

- (a) the security is indorsed by the appropriate person or persons, (Sec. 8-308); and
- (b) reasonable assurance is given that those indorsements are genuine and effective (Sec. 8-402); and
- (c) the issuer has no duty to inquire into adverse claims or has discharged any such duty (Sec. 8-403); and
- (d) any applicable law relating to the collection of taxes has been complied with; and
- (e) the transfer is in fact rightful or is to a bona fide purchaser.

(2) Where an issuer is under duty to register a transfer of a security the issuer is also liable to the person presenting it for registration or his principal for loss resulting from any unreasonable delay in registration or from failure or refusal to register the transfer. § 8-402 (1) The issuer may require the following assurance that each indorsement is genuine and effective

- (a) in all cases, a guarantee of the signature (sub-section (1) of Section 8-312) of the person indorsing; and
- (b) where the indorsement is by an agent, appropriate assurance of authority to sign;
- (c) where the indorsement is by a fiduciary, an appropriate certificate of appointment or incumbency dated within sixty days of the date of presentation for transfer;
- (d) where there is more than one fiduciary, reasonable assurance that all who are required to sign have done so;
- (e) where the indorsement is by a person not covered by any of the foregoing, assurance appropriate to the case corresponding as nearly as may be to the foregoing.

(2) A "guarantee of signature" in subsection (1) means a guarantee signed by or on behalf of the person reasonably believed by the issuer to be responsible. The issuer may adopt standards with respect to responsibility provided such standards are not manifestly unreasonable.

(3) "An appropriate certificate of appointment or incumbency" in subsection (1) means

- (a) in the case of a fiduciary appointed or qualified by a court, a certificate issued by or under the direction or supervision of the court; and
- (b) otherwise, a certificate issued by or on behalf of a person reasonably believed by the issuer to be qualified so to certify. The issuer may adopt standards with respect to qualification provided such standards are not manifestly unreasonable.

(4) If the issuer has notice that the transfer may be wrongful, it may require reasonable assurance beyond that specified in this section. But if an issuer elects to investigate the requested transfer and both requires and obtains a copy of a will, trust, indenture, articles of co-partnership, by-laws or other controlling instrument it is put on notice of all matters contained therein affecting the transfer.

§ 8-403 (1) An issuer to whom a security is presented for registration is under a duty to inquire into adverse claims if

a security transfer. These provisions it appears, do little to resolve the problem of simplification. Experience has shown that in Pennsylvania the Uniform Commercial Code has done little to simplify, or even make uniform throughout the state, the requirements of documentation.²⁰

Many states have attempted to solve the problem of simplification by means of "nominee statutes"²¹ which authorize a fiduciary to nominate a third person to hold securities in the third persons name without giving notice, on the stock certificate or on the transfer books of the corporation of his qualified ownership.²² ". . . the acts leave many categories of transfers wholly unsimplified, and in those categories which are simplified, the acts substitute a lesser evil for a greater rather than eliminating both."²³

The Model Fiduciaries Securities Transfer Act was promulgated by the Committee on Simplification of Security Transfers by Fiduciaries, formed in 1951 within the Section of Real Estate, Probate, and Trust Law of the American Bar Association. It won adoption in two states.²⁴ Barely had its ink had time to dry when it was

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- (a) a notification of an adverse claim is received at a time and in a manner which affords the issuer a reasonable opportunity to act on it prior to the issuance of a new, reissued or re-registered security; or
 - (b) the issuer has notice of an adverse claim by electing to require a controlling instrument as provided in the last subsection of the preceding section.
 - (2) The issuer may discharge any duty of inquiry by any reasonable means, including notifying an adverse claimant by registered or certified mail at the address furnished by him or if there be no such address at his residence or regular place of business that the security has been presented for registration of transfer by a named person, and that the transfer will be registered unless within thirty days from the date of mailing the notification, either
 - (a) an appropriate restraining order, injunction or other process issues from a court of competent jurisdiction; or
 - (b) an indemnity bond sufficient in the issuer's judgment to protect the issuer and any transfer agent, registrar or other agent of the issuer involved, from any loss which it or they may suffer by complying with the adverse claim is filed with the issuer.
 - (3) Except to the extent that an issuer has notice by electing to require a controlling instrument as provided in the last subsection of the preceding section or receives notification of an adverse claim under subsection (1) of this section, where a security presented for registration is indorsed by the appropriate person or persons the issuer is under no duty to inquire into adverse claims. In particular
 - (a) an issuer registering a security in the name of a fiduciary is not bound to inquire into the existence, extent, or correct description of the fiduciary relationship;
 - (b) an issuer registering transfer on an indorsement by a fiduciary is not bound to inquire whether the transfer is made in compliance with a controlling instrument or with the law of the state having jurisdiction of the fiduciary to obtain court approval of the transfer; and
 - (c) the issuer is not charged with notice of the contents of any court record or file or other recorded or unrecorded document even though the document is in its possession and even though the transfer is made on the indorsement of a fiduciary to the fiduciary himself or to his nominee.

20. Conrad, *supra* note 6, at 849.

21. N.D. Rev. Code §§ 10-1822-23 (Supp. 1957).

22. A study and comparison of the various nominee statutes is found in 56 Mich. L. Rev. 963.

23. Conrad, *supra* note 6, 851.

24. Del. Laws 1957, S. B. 287; Ill. Rev. Stat. c. 32, §§ 439.50-439.57 (1957). Also enacted in Connecticut, with changes; Conn. Pub. Acts, 1957, No. 573.

followed by the Uniform Act for Simplification of Fiduciary Security Transfers, the work of the National Conference of Commissioners on Uniform State Laws. This act, approved by the commissioners in 1958, is the latest step in the simplification drive. The only differences between the two acts appear to be technical and terminological, arising from the commissioners insistence on conformity to style of previous uniform laws.²⁵

The Uniform Act for Simplification of Fiduciary Transfers provides that a corporation or transfer agent making a transfer may assume without inquiry that the assignment, even though to the fiduciary himself or his nominee, is within his authority and capacity and is not in breach of his fiduciary duty.²⁶ It may also be assumed without inquiry that the fiduciary has complied with the controlling instrument and with the law of the jurisdiction governing the fiduciary relationship, including any law requiring the fiduciary to obtain court approval of the transfer.²⁷

The corporation or transfer agent is not charged with notice of and is not bound to obtain or examine any court record or any recorded or unrecorded document relating to the fiduciary relationship or the assignment, even though the record or document is in its possession.²⁸

It is further provided that a person asserting a claim may give written notice to the corporation or transfer agent, and the character and effect of such notice are dealt with.²⁹ A corporation or transfer agent incurs no liability to any person by making a transfer or otherwise acting in a manner authorized by the act.³⁰

Other sections provide for registering securities in the name of the fiduciary and for assumption, without inquiry, of the continuance of the fiduciary status.³¹ A simple system of evidence of appointment is provided for; if appointed by a court, a certificate of the court dated within 60 days previous to the application for transfer. If appointed otherwise, a document showing appointment.³²

Non-liability of third persons, including the signature guarantor,

25. Conrad, *supra* note 6, 883.

26. UNIFORM ACT FOR SIMPLIFICATION OF FIDUCIARY SECURITY TRANSFERS, § 3 (a).

27. *Ibid.*, § 3 (b).

28. *Ibid.*, § 3 (c).

29. *Ibid.*, § 5.

30. *Ibid.*, § 6. There is no exception for cases of "actual knowledge" or "bad faith" as in § 3 of the UNIFORM FIDUCIARIES ACT.

31. *Ibid.*, § 2.

32. *Ibid.*, § 4.

in the absence of actual knowledge of the breach, is provided.³³ Tax obligations are unaffected.³⁴

A possible question of conflict of laws is eliminated by a provision that the rights and duties of a corporation and its transfer agent are governed by the laws of the state of incorporation.³⁵ This makes it unnecessary for the transfer agent to look to the laws of any other state. If the state of incorporation has adopted the Uniform Act, the transfer can be safely registered though other states having contact points³⁶ may not have adopted the act.

This then is the situation: Despite previous acts aimed at simplification by reducing the liability of corporations and their transfer agents, the courts have continued to impose a rather strict duty of care upon transfer agents. Leading authorities have been nearly unanimous in their demands for simplification. The Uniform Act for Simplification of Fiduciary Security Transfers appears to represent about the ultimate in simplification by reducing liability. Just how the courts will interpret the act when it is adopted remains to be seen. Simplification of transfers must be weighed against the welfare of remaindermen, infants, decedents estates etc., and a proper balance struck.

A viewpoint often overlooked in the press for simplification, but ever present, was stated thus: "Often the advocates of simplified stock transfers point to the Uniform Fiduciaries Act and similar statutes and, in effect, say the transfer agent should be put on a blind bridle and run rough-shod over possible rights of widows and children. No bank wants to be associated with a breach of trust, whether or not it can be held liable."³⁷

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33. *Ibid.*, § 7. The term "actual knowledge" used in the UNIFORM FIDUCIARIES ACT is retained.

34. *Ibid.*, § 9. That this was also so under the UNIFORM STOCK TRANSFER ACT, see, *Hiller v. A. T. & T. Co.*, 324 Mass. 24, 84 N.E.2d 548 (1949).

35. *Ibid.*, § 8.

36. Other contact points may be: (1) the state of transfer. (2) the state of fiduciary administration. For a discussion of conflict problems, see, Conrad, *supra* note 6, 869.

37. Williams, *Easing Problems of Stock Transfers*, 73 Banking L. J. 457, 459 (1956).