

June 30, 2010

**Maryland Legislature Approves Changes to Maryland Business Trust Act  
(retitled the Maryland Statutory Trust Act)**

The Maryland General Assembly has substantially revised Title 12 of the Corporations and Associations Article of the Annotated Code of Maryland, which was formerly the Maryland Business Trust Act and is now the Maryland Statutory Trust Act (the "Act"). Senate Bill 784 was signed into law by the Governor of Maryland on May 20, 2010 and became effective June 1, 2010. These amendments were proposed and drafted by the Corporate Laws Committee of the Business Law Section of the Maryland State Bar Association.

While the amendments do not generally affect the opportunity for free writing in the Act as originally enacted in 1999, they make many clarifications and revisions and add new default provisions for matters not addressed in the declaration of trust, bylaws or other governing documents (collectively, the "Governing Instrument") or in the certificate of trust (the "Certificate of Trust") filed with the State Department of Assessments and Taxation (the "SDAT"). The summary below discusses the most significant changes. Unless otherwise noted, all section references below are to the Act.

*BUSINESS TRUSTS FORMED IN MARYLAND ON OR BEFORE MAY 31, 2010*

No immediate action is required of business trusts already formed in Maryland. Pursuant to Section 12-101(h)(2), the term "statutory trust" includes a trust formed under Title 12 on or before May 31, 2010, as a "business trust" as that term was then defined in Title 12. Accordingly, no election, filing or other immediate action is required by a trust that was formed under the former Business Trust Act. Also, as the Act contains few mandatory requirements, it is therefore very unlikely that any existing provisions of the Certificate of Trust or Governing Instrument are substantively affected by the revisions to the Act. However, where the Governing Instrument is silent on a matter, a new statutory default may govern. It would be prudent to review the Certificate of Trust and Governing Instrument of any trust formed under the Business Trust Act to determine whether any changes are advisable.

*FOREIGN STATUTORY TRUSTS—QUALIFICATION TO DO BUSINESS IN MARYLAND*

A foreign statutory trust may need to qualify to do business in Maryland. The Act provides for such qualification, which was not addressed in the Business Trust Act. Under Section 12-101(d), a "foreign statutory trust" is a trust formed under the laws of another state or jurisdiction and is "required by the laws of the jurisdiction in which it is formed to file a record with a public official in that jurisdiction." New Subtitle 9 sets forth the requirements regarding qualification and Section 12-908(a) lists activities that do not constitute doing business in Maryland. Section 12-908(b) provides that:

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In addition to any other activities which may constitute doing business in this State, for the purposes of this subtitle, a foreign statutory trust that owns income producing real or tangible personal property in this State, other than property exempted by subsection (a) of this section, shall be considered to be doing business in this State.

Accordingly, subject to limited exceptions, any foreign statutory trust owning income producing property in Maryland should register to do business in the state.

#### *ORGANIZATION*

The amendments change the name of an entity formed under the Act from "business trust" to "statutory trust" and conform references throughout. Section 12-104 is amended to change the short title of the statute to the Maryland Statutory Trust Act.

The definition of statutory trust is amended to clarify that a statutory trust is formed by filing a Certificate of Trust with the SDAT under Section 12-204. Prior to the amendments, the statute contained some ambiguity as to whether the trust was formed under the Governing Instrument or by the filing of the Certificate of Trust.

#### *INTERPRETATION OF THE ACT—FREEDOM OF CONTRACT*

New Section 12-105 clarifies that the Act shall be liberally construed to give maximum effect to the principle of freedom of contract and to the enforceability of Governing Instruments. Section 12-105 further clarifies that, to the extent that the Act overrides common law trust principles, it should not be construed strictly. These changes reinforce the free-writing aspect of the Act and further distinguish statutory trusts from trusts formed under common law.

New Section 12-101.1 provides that the use of the term "business trust" prior to June 1, 2010 does not create a presumption that the trust is a business trust under federal bankruptcy law.

#### *POWERS OF THE TRUST*

Section 12-201(c) adds a list of general powers, which are generally consistent with the powers provided for a Maryland corporation under the Maryland General Corporation Law (the "MGCL"), thus avoiding any argument that a detailed description of trust powers needs to be included in the Certificate of Trust or the Governing Instrument. These powers may be limited in the Certificate of Trust or the Governing Instrument.

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*GOVERNING INSTRUMENT*

Section 12-207(b) contains a number of permissive provisions that may be included in the Governing Instrument. The Act also includes amendments expanding the list of permissive provisions in order to clarify the treatment of certain subjects. For example, Section 12-207(b)(3) states that the Governing Instrument may provide for a fixed or unlimited number of shares or other units of beneficial interest or for a combination of shares or other units of beneficial interest in the statutory trust and Section 12-207(b)(9) states that the Governing Instrument may provide rights for any person, including a person not a party to the Governing Instrument, to the extent set forth in the Governing Instrument.

*TRUSTEES*

The amendments to Section 12-402 expressly provide for duties of trustees that are the same as those of directors of a Maryland corporation under the MGCL, except as modified in the Governing Instrument. Specifically, Section 12-402 provides that:

(b) Subject to subsection (c) of this section, a trustee shall perform the trustee's duties as a trustee, including the duties as a member of a committee of the trustees on which the trustee serves:

(1) in good faith;

(2) in a manner that the trustee reasonably believes to be in the best interests of the statutory trust; and

(3) with the care that an ordinarily prudent person in a like position would use under similar circumstances.

(c) The governing instrument of a statutory trust may include a provision expanding or limiting the duties of a trustee set forth in subsection (b) of this section, provided that the governing instrument may not eliminate the duty to act in good faith.

The amendments provide greater clarity regarding the duties of trustees and the way in which they may be expanded or limited in the Governing Instrument.<sup>1</sup> Even the

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<sup>1</sup>The Act formerly provided that a trustee shall have no duty or liability to the trust or a beneficial owner for any act greater than that of directors of a Maryland corporation to the corporation, in the absence of any provision in the Governing Instrument. Thus, there was some ambiguity as to how the duties of trustees could be varied in the Governing Instrument. In the unlikely event that an existing Governing Instrument purports to eliminate a trustee's

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reasonable belief and ordinary prudence duties may be eliminated. The amendments also provide that a trustee has no duties other than as set forth in the Act, as modified in the Governing Instrument. Thus, unless the Governing Instrument expressly provides otherwise, the Act eliminates all common law duties of trustees as well as any opportunity for courts to create additional state law duties.

Section 12-403 is amended to clarify that, except as provided in the Governing Instrument, a statutory trust may indemnify and advance expenses to its trustees, officers, employees or agents.

Additionally, a new Section 12-405 provides that a trustee of an investment company formed as a statutory trust who with respect to the statutory trust is not an "interested person," as defined by the Investment Company Act of 1940, shall be deemed to be independent and disinterested when making determinations or taking actions as a trustee. This provision is consistent with Section 2-405.3 of the MGCL for directors of investment companies incorporated in Maryland.

#### *BENEFICIAL OWNERS*

Section 12-301 is amended to clarify what may constitute valid consideration to be paid or provided to the statutory trust for a beneficial interest in a statutory trust. The amendments also clarify that, except as provided in the Governing Instrument or by agreement, a beneficial owner has no preemptive right to acquire any beneficial interest or other interest in the statutory trust. Section 12-101 is also amended to clarify that a beneficial owner means any owner of record of a beneficial interest in a statutory trust.

Section 12-304 is amended to clarify that a statutory trust has the power, except as provided in the Governing Instrument, to pay or reimburse, in advance of final disposition of a legal proceeding, any expenses incurred by a beneficial owner in connection with the proceeding.

#### *MEETINGS OF TRUSTEES AND OF BENEFICIAL OWNERS*

New Section 12-404 governs (a) meetings of trustees, (b) the taking of action by trustees by consent without a meeting and (c) voting by trustees by proxy. New Section 12-306 governs (a) meetings of beneficial owners, (b) the taking of action by beneficial owners by consent without a meeting and (c) voting by beneficial owners by proxy. These default provisions are analogous to provisions in the MGCL for directors and stockholders of Maryland

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duty to act in good faith, the amendments to the Act would override such provision -- the only instance in which the amendments affect an existing provision of a Governing Instrument.

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corporations (except that the MGCL does not permit a director to act by proxy). These defaults may be modified in any respect in the Governing Instrument.

*MERGER OR CONSOLIDATION; DISSOLUTION*

The amendments to the Act clarify certain provisions of Subtitle 6, which governs a merger or consolidation of a statutory trust with another entity. Additionally, the amendments eliminate certain required information from articles of merger or consolidation filed with the SDAT. The amendments also expressly provide for the dissolution of a series or class of beneficial interests of a statutory trust without dissolution of the entire entity.

*CONSENT TO JURISDICTION*

Section 12-501(b) is amended to clarify that a trustee, beneficial owner or other person may consent in the Governing Instrument or other writing to be subject to, among other things, the exclusive jurisdiction of the courts of Maryland or the exclusivity of arbitration in a specified jurisdiction.

*COMPARISON TO THE DELAWARE STATUTORY TRUST ACT*

While the Act is substantially comparable to the Delaware Statutory Trust Act, there are noteworthy differences, including the following:

1. The Act requires a resident agent in Maryland but does not require a trustee in Maryland. For trusts that are not investment companies, the Delaware statute requires at least one trustee who is a resident of Delaware or has its principal place of business in Delaware.
2. The Act includes an extensive list of general trust powers as noted above. The Delaware statute contains no such provision (although there is no statutory limitation on a trust having such powers).
3. The Act states that the Governing Instrument may provide for the division of beneficial interests in the trust into a fixed or unlimited number of shares or other units or the combination of shares or other units of beneficial interests. The Delaware statute has no such provision (although there is no statutory limitation on inclusion of such provisions in the Governing Instrument).
4. The Act contains the default standard of the MGCL for the duties of trustees as described above. In Delaware, the default duties of trustees are the duties established at law or in equity, including fiduciary duties. While the Act provides that all trustee duties, but for the duty to act in good faith, may be eliminated in the Governing Instrument, the Delaware statute permits limitation of trustee duties, except for the implied contractual covenant of good faith and fair

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dealing. "Good faith" has been the subject of extensive litigation in the Delaware courts in the past 15 years.

5. Under the Act, the Governing Instrument may limit the liability of the trustees, except for liability resulting from (a) actual receipt of an improper benefit or profit in money, property or services or (b) active and deliberate dishonesty established by a final judgment as being material to the cause of action. In Delaware, the Governing Instrument may eliminate trustee liability, except for liability for "any act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing."

6. Although the Act does not provide for the conversion of statutory trusts, it does provide, as noted above, for merger or consolidation. The Delaware statute provides for the conversion of statutory trusts.

7. The Act does not confer on a beneficial owner a right to bring a derivative action. The Delaware statute confers a right to bring a derivative action on a beneficial owner if the trustees have refused to bring the action or are not likely to do so, which is a more expansive right to sue derivatively than the Maryland courts have permitted.

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We believe that the amendments contained in the Act enhance the utility of the Maryland Statutory Trust as a form of doing business for registered investment companies -- especially mutual funds and exchange-traded funds -- for private funds and in real estate and other transactions. The three of us were actively involved in the drafting and development of this legislation on behalf of the Bar Association, and Michael Leber provided testimony to the General Assembly in support of the amendments. As always, please do not hesitate to call any of us or any of our colleagues if you have any questions or comments about any of the foregoing or any other matter of Maryland law.

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*This memorandum is not intended to provide legal advice or opinion. Such advice may only be given when related to specific fact situations for which Venable LLP has accepted an engagement as counsel to address.*