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Trusts--Insolvent Banks--Tracing Trusts Property

TRUSTS—INSOLVENT BANKS—TRACING TRUST PROPERTY—April 18, 1930, the City Trust Company, as executor of the will of James Fordice French, paid over to itself as trustee under a trust created by the same will, the sum of $90,000 in cash. This money was commingled with all other money in the hands of the Company and turned over to the banking department as cash. All but $38,679.68 was invested by the Company for the benefit of the trust. October 23, 1930, the City Trust Company went into hands of a receiver with cash on hand amounting to $18,255.76. The cash on hand was never less than that amount after the trust fund was deposited. Claimant is the duly appointed present trustee of the French trust and claims a pre-

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[9] Note 4, *supra*.
[10] (1910) A. C. 27.

ferred claim to the extent of $38,679.68 upon all funds in the hands of the receiver of the City Trust Company. *Held*, that there was a preferred claim to the extent of $18,255.76 which was the largest sum that could be presumed to have remained in the hands of the Company from the deposit on April 18, 1930, that augmented the assets that passed into the hands of the receiver. Judgment for the claimant, reversed in part.[1]

The relationship of debtor-creditor was never created between the two departments of the City Trust Company. The method of keeping books could not in any way jeopardize the rights of the beneficiary under the trust.[2]

It is agreed in all cases and authorities that if a trustee becomes insolvent with trust property in his hands and the trust property can be traced ino the hands of the receiver that the *cestui que trust* is entitled to a preferred claim against the assets held by the receiver. The dispute is as to what constitutes a sufficient tracing of the trust property into the hands of the receiver. There are three distinct rules on this point. The most strict rule is that the identical, particular, and specific property has to be found in the receiver's hands so as to directly augment the assets held by him. Under this strict rule it would be practically impossible to get a preferred claim in case of money being the trust property. To prove such claim it would necessitate earmarking the specific coins or bills or taking the numbers of the bills. The operative effect of this rule seems to be that as soon as the trust money is commingled with the trustee's own money, no matter what the proportion is, so that the strict identity is lost, and the trustee goes into receivership, the trust money is no longer trust money and the relation between the receiver and the beneficiary becomes debtor-creditor.[3]

In extreme contrast to the strict rule there is the very liberal rule which presumes, after the trust is proven, that the property has gone into the hands of the receiver and has increased the assets held by him. The practical result of this rule is that no tracing is required at all after the trust is proven. However, it is held that the presumption is a rebutable one and if it is shown that the original trust fund could not possibly have gone into the hands of the receiver no preferred claim will be allowed.[4]

The decided weight of authority adopts the rule as set out in the principal case. It is a more moderate view than the two extreme rules set out above. This rule requires that there be a substantial identification of the trust property, and in case it consists of money, the identical coins or bills do not have to be traced, but only the original trust money as a fund has to be identified. The operative effect of this rule, as in the principal case, is

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[1] *Rottger v. First-Merchants' Nat'l Bank of Lafayette,* Appellate Court of Indiana, Jan. 31, 1933, 184 N. E. 267.

[2] *Terre Haute Trust Co. v. Scott,* and cases cited. (1932) 181 N. E. 369.

[3] Perry, Trusts, 836, 1916C, L. R. A. 21, Exhaustive note on subject; *Byrne v. Byrne* (1896), 113 Cal. 294, 45 Pac. 536; *Mathewson v. Wakelee* (1910), 83 Conn. 75, 75 Atl. 93; *Collins v. Steuart* (1899), 58 N. J. Eq. 392, 44 Atl. 467; *Davis v. Shepard* (1925), 135 Wash. 124, 237 Pac. 21.

[4] *McLeod v. Evans* (1886), 66 Wis. 401, 28 N. W. 173. This is the leading case on this view but it is expressly overruled in Wisconsin by *Nonotuck Silk Co. v. Flanders* (1894), 87 Wis. 237, 58 N. W. 383; *Myers v. Board of Education* (1893), 51 Kan. 87, 32 Pac. 658, 37 Am. St. Rep. 263; *State v. Bruce, Rec.* (1909), 17 Idaho 1, 102 Pac. 831, 1916C, L. R. A. 1; *Eastman v. Farmers' State Bank* (1928), 175 Minn. 336, 221 N. W. 236.

that the lowest cash on hand held by the trustee from the time he acquires the trust money to the time he goes into receivership will be the largest sum that will be presumed to have remained of the original trust money that passed into the hands of the receiver.[5]

The law in Indiana on this subject of tracing misappropriated trust funds has gone through an evolution and period of growth before the rule as announced in the principal case was reached. The first case found on the subject stated a rule which sounds like the strict doctrine, as it was said that if the trustee did not preserve the identity as well as the existence of the funds and if he paid out the money as his own, the trust is practically at an end.[6] However, it was only a few years later that the extreme strictness was taken out of the rule as first stated and the property in which the trust fund was wrongfully invested was subjected to the trust.[7] This case is the basis of the modern Indiana law as to tracing trust property. Later in the same year the court went back to the strict view by requiring the trust fund to be "distinctly identified,"[8] but this limitation was impliedly repudiated in still later cases which adopted the rule as stated in the previous case.[9]

The first case involving a bank as trustee, as in the principal case, was one in the Appellate Court.[10] In this case the Indiana rule as set out in the principal case was stated. Two years later the Supreme Court adopted the same rule in the same general language though it did not cite this case. Thus at this early date, the Indiana rule was apparently settled with the cases immediately following in accord.[11] But in the next several years there are a number of cases in point and several follow the supposedly settled rule[12] but as pointed out in the principal case there are some that tend to deviate. Two of the decisions tend to support the old strict rule as to confusion of goods,[13] while another states the liberal view and cites together *McLeod v. Evans*, which is the leading authority on the liberal rule, and

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[5] *Albert Pick & Co. v. Union Trust & Savings Bank* (1923), 196 Iowa 706, 195 N. W. 378, 31 A. L. R. 466; *Nonotuck Silk Co. v. Flanders, supra,* note 4; *Massey v. Fisher* (1894), 62 Fed. 958; *Smith v. Fuller* (1912), 86 Ohio St. 57, 99 N. E. 214, 1916C, L. R. A. 6; *Kent v. Kent* (1917), 50 Utah 44, 165 Pac. 271; *Central Nat. Bank v. First Nat. Bank* (1927), 115 Nebr. 444, 213 N. W. 745, 216 N. W. 302; *Leach v. Iowa State Sav. Bank* (1927), 204 Iowa 497, 215 N. W. 728; *City of Lincoln v. Morrison* (1902), 64 Nebr. 822, 90 N. W. 905; *In re Arms' Estate* (1921), 186 Cal. 554, 199 Pac. 1053; *Schuyler v. Littlefield, Trustee* (1914), 232 U. S. 707, 58 L. Ed. 806, 34 S. Ct. 466; *St. Louis, etc., Co. v. Spiller* (1927), 274 U. S. 304, 71 L. Ed. 1060, 47 S. Ct. 634.

[6] *State v. Sanders* (1878), 62 Ind. 562.

[7] *Bundy, Rec., v. The Town of Monticello* (1882), 84 Ind. 119.

[8] *McComas v. Long* (1882), 85 Ind. 549.

[9] *Riehl v. The Evansville Foundry Assoc.* (1885), 104 Ind. 70, 3 N. E. 633; *Rowley, Adm., v. Fair* (1885), 104 Ind. 189, 3 N. E. 860; *Orb v. Coapstick* (1893), 136 Ind. 313, 36 N. E. 278.

[10] *Windstanley v. Second National Bank* (1895), 13 Ind. App. 544, 41 N. E. 956.

[11] *Pearce v. Dill* (1897), 149 Ind. 136, 48 N. E. 788.

[12] *Shepard, Trustee, v. The Meridian Nat'l Bank* (1897), 149 Ind. 532, 48 N. E. 346; *Union Nat'l Bank v. Citizens Bank* (1899), 153 Ind. 44, 54 N. E. 97; *Hanna v. McLaughlin* (1901), 158 Ind. 292, 63 N. E. 475; cited in dissenting opinion—*Miller v. Stephenson* (1901), 27 Ind. App. 271, 59 N. E. 398; *Porter v. Roseman* (1905), 165 Ind. 255, 74 N. E. 1105, 112 Am. St. Rep. 222, 6 Ann. Cas. 718.

[13] *Indiana Trust Co. v. International Building & Loan Assoc.* (1905), 165 Ind. 597, 76 N. E. 304; *Reserve, etc., Ins. Co. v. Dulin, Rec.* (1924), 82 Ind. App. 630, 135 N. E. 90.

the *Windstanley* and *Shopert* cases as stating the same rule.[14] Thus the law that was supposedly settled became again unsettled. With the law in this state, in a relatively recent case, the Supreme Court definitely adopted the rule as stated in the *Windstanley case*[15] and the later cases have followed this view.[16] In one case the opinion is misleading as to which rule is being followed but the result seems to be in accord with the settled view.[17] At the present time the law in Indiana on this point is apparently settled as stated in the principal case as to banks acting as trustee and becoming insolvent before March 11, 1931. If any bank acting as trustee should become insolvent after that date, a statute declares that the fund held in trust shall be a preferred claim over general creditors.[18] There is a more recent case which cites with approval the principal case without stating its holding.[19] J. W.

WORKMAN'S COMPENSATION—ARISING OUT OF THE EMPLOYMENT—The appellant alleged that, on the 14th day of April, 1931, he received certain personal injuries by reason of an accident arising out of and in the course of his employment in the appellee's factory, by reason of which he lost his left eye. When no agreement, as to compensation, could be reached, the appellant filed his application with the Industrial Board, on account of said injuries, on the 5th day of June, 1931, and was heard by a single member of the board, who found in favor of the appellant. The appellee on the 28th day of October, 1931, filed an application for a review by the full board, which found that the appellant's alleged accidental injury was not the result of an accident arising out of and in the course of his employment. The appellant appealed, assigning as error that "the finding and order of the Full Industrial Board is contrary to law." *Held*, the accidental injury did not cause the disability of the appellant.[1]

The court, without an analysis of the causal relation of the accident, the injury and the employment, affirmed the award of the Industrial Board by following the rule, that, where there is some evidence to support the finding, the award is conclusive, if there has been proper notice and a full

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[14] *State v. Farmers & Merchants Nat. Bank* (1919), 71 Ind. App. 216, 124 N. E. 501.

[15] *Fletcher Savings & Trust Co. v. American State Bank* (1925), 196 Ind. 118, 147 N. E. 524.

[16] *Crowder, Rec., v. Sandusky* (1929), 91 Ind. App. 200, 170 N. E. 792; *Allen & Steen Acceptance Co. v. Cook, Rec.* (1930), 93 Ind. App. 682, 173 N. E. 460; *Crowder v. Abbott* (1931), 178 N. E. 860; *Mock v. Stultz* (1932), 179 N. E. 561; *Terre Haute Trust Co. v. Scott* (1932), 181 N. E. 369.

[17] *Stults, Rec., v. Gordon, Adm.* (1929), 89 Ind. App. 611, 167 N. E. 564.

[18] Acts 1931, Chapter 167, page 580. That hereafter, upon the insolvency, suspension or liquidation of any bank of discount and deposit, or loan and trust and safe deposit company, while acting as executor, administrator, receiver, guardian, assignee, commissioner, agent, attorney-in-fact, or in any other fiduciary capacity, the person or persons beneficially entitled to receive the property and proceeds held in trust by it as aforesaid, or its successors in trust, shall have preference and priority over its general creditors in all assets of such bank or loan and trust and safe deposit company, for all uninvested funds so held in trust to the extent of any commingling with its general assets or which may not be duly accounted for.

[19] *Rottger v. Delta Delta Delta Realty Corporation* (1933), 184 N. E. 412.

[1] *Hess v. Ohlen Bishop Co.*, Appellate Court of Indiana, Dec. 15, 1932. 183 N. E. 387.