Opinion No. 60-09

January 20, 1960

BY: OPINION of HILTON A. DICKSON, JR., Attorney General

TO: Mr. Jack Hester State Investment Officer P. O. Box 1356 Santa Fe, New Mexico

QUESTION

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Is the action of the State Investment Council, in entering into an agreement with certain investment banking firms to exchange presently held municipal bonds for Government bonds, legal considering the following points:

1. Does the agreement violate § 11-2-8.10, N.M.S.A., 1953 Compilation (P.S.)?

2. Does the Council have the authority to sell or trade securities which were in the State portfolio at the time the Council was established?

3. Is the Council's action in entering into the agreement illegal under § 11-2-8.14, N.M.S.A., 1953 Compilation (P.S.)?

4. Is the agreement in violation of the rule against a trustee intermingling trust funds?

5. Is the contract a legal and enforceable agreement?

CONCLUSION

Yes.

OPINION

*{*346}* **ANALYSIS**

We have taken the liberty of rewording your request so that all possible legal questions which occur to us may be resolved.

At the outset, it should be pointed out that this opinion will be limited to the bare legal questions involved and will in no way attempt to rule on the propriety of the proposed action by the Council since it is not the function of this office to attempt to replace the Council's judgment and administrative action with our own. This opinion will not evaluate the benefit or detriment to the State under the proposed plan except insofar as to determine whether the Council has acted so arbitrarily and capriciously as to amount to a prima facie violation of its investment standards.

1. The first question presented for our consideration is whether the proposed contract violated § 11-2-8.10, supra, which reads, in germane part, as follows:

"Securities or investments purchased or held may be sold or exchanged for other securities and investments; **Provided, however, that no sale or exchange shall be at a price less than the going market at the *{*347}* time the securities or investments are sold or exchanged."** (Emphasis supplied)

It seems clear that the requirement of this section, as it pertains to an exchange, is that the securities which are to be received in the exchange must have an aggregate price which is equal to or in excess of the market price of the securities which are to be given by the State. The application of these words to the present proposal is somewhat more difficult.

The exact market price of the Government bonds to be received is, of course, easily ascertainable. The market price of the municipal bonds which are to be given is extremely difficult to ascertain. The problem which presented itself to the Council was for the Council to make a determination of what, in fact, was the market price of the municipal bonds so that a determination could be made as to whether the municipal bonds were being traded at less than the going market price. The Council has stated to this office that as a matter of administrative determination it has concluded that they are receiving bonds which have a market price equal to or in excess of the market price of the municipals. This statement by the Council must be taken at its face value and it is not the function of this office to question whether such a determination was correctly made. The only examination this opinion will make into the ascertainment of the market price of the bonds is to determine whether the Council acted in good faith in arriving at its conclusion as to the price and did not act arbitrarily and capriciously.

The term "market price" has been the subject of many comments by the courts of the several states. The generally accepted definition or meaning would seem to indicate that the words imply price or value in an open market where one desires but is not compelled to buy and one is willing but not compelled to sell. In order for an item to have a market price, the same or similar items must have been sold enough times so that the items obtain a somewhat fixed price or value to purchasers. Many courts have held that where the market price cannot be established by prior sales, other criterion than an active market must be considered so that a price is estimated which would represent a fair price arrived at by negotiation by a buyer willing to purchase and a seller willing to sell. Courts express the view that it is as difficult to determine what should be taken into consideration in determining market price as it is difficult to determine market price itself. **Hemler v. Union Producing Company,** 40 Fed. Supp. 824; **Butler v. Aetna Ins. Co.,** 64 N.D., 764, 256 N.W. 214. Somewhat the same view is expressed by the Supreme Court of New Mexico in **Ford v. Norton et al.,** 32 N.M. 518, 260 P. 411, wherein the Court, while indicating that the best evidence of market price is actual sales, acknowledges that actual sales do not always exist. Without an actual market, the test of market price becomes subjective rather than objective in giving due consideration to many factors which influence an item's value or merchantability.

Upon the holding of the cases on this subject, of which the cited cases are but an indication, and the facts of the present proposal, we are unable to say that the Council did not act in good faith in arriving at its conclusion, nor are we in a position to say that the Council did not consider all the things persons normally consider in arriving at a market price when no established market is available.

On this point, we are constrained to uphold on a legal basis the action of the Council as a good faith determination of market price so that substantial compliance with the statute has been effected.

2. We turn now to the question of whether the Council has the power and authority to sell and exchange securities which were in *{*348}* the State portfolio at the time the Council was created. To answer this question, we must turn to trust law since it is our feeling that the position of the Council is analogous to, if not, in fact, one of a trustee.

From our examination of the state of the law on the question of whether a trustee can sell or exchange securities delivered to him upon initiation of the trust, the rule generally is that unless the instrument creating a trust confers the power upon the trustee to take such action, he cannot do so without an order of a court. See in this connection C.J.S., Trusts, Volume 90, § 286, at page 417, and 57 A.L.R. 1118. The cases hold, however, that under certain trust instruments conferring broad powers, the trustee has such a right under that grant of power. **Bradford et al. v. Shakespeare,** 126 N.J. Equity 321, 8 A. 2d 784; **Crutcher v. Joyce,** 134 Fed. 2d 809. We must, therefore, examine the instrument creating the trust -- in this case the statute -- to determine whether such power was granted. Section 11-2-8.10, supra, confers the power upon the Council and Investment Officer. It provides, in part, as follows:

"Subject to the limitations, conditions and restrictions contained in policy making regulations or resolutions promulgated by the council with the approval of the financial officer, and subject to prior authorization by the council, **the state investment officer shall have the power to make purchases, sales, exchanges, investments and reinvestments of the permanent state fund.** The state investment officer is charged with the duty of seeing that moneys invested are at all times handled to the best interests of the state." (Emphasis supplied)

The above underscored portion of the statute, in our opinion, specifically confers upon the Investment Officer the power to sell and exchange securities originally held in the State portfolio. It contains no restrictions on which securities may be sold or exchanged. This view is strengthened when we recall that the primary purpose for the creation of the Council was to improve the position of the Permanent Fund in regard to its investments generally, and specifically, its return on the funds invested, keeping in mind, of course, the preservation of the principal. This goal could hardly be accomplished if the powers of the Council were limited to investing only current funds.

If the present proposal under consideration involved an attempt by the Council to dispose of originally held securities which were clearly and rapidly deteriorating in value,

little doubt if any, would be expressed that the Council had the right so to act. Indeed, it might be said that the Council had the duty under its investment standard so to act.

As a legal matter and not one of propriety, we are unable to distinguish the two situations. Upon the broad powers conferred by the statute having no express limitation as to which securities may be sold or exchanged, we are constrained once again to uphold the action of the Council as lawful in this regard.

3. The third point concerns whether the Council, upon entering into this agreement of exchange, acted so arbitrarily and capriciously and without regard for the interests of the State so as to amount to an unlawful act.

Much has been said of the propriety of the contemplated exchange. Many laymen and securities authorities have expressed their opinions with the result that very few agree exactly on the effect of the exchange. The Council being an executive panel should and will here be given the benefit of the presumption of validity, due diligence and good faith devotion to duty to which it is rightfully entitled. Since even the experts are in disagreement -- some in favor *{*349}* and some not -- we cannot say without substantially more evidence of bad faith and nondiligence that the Council acted outside the standard of conduct of a reasonably prudent investor as set by statute.

Until a positive showing is made to this office that the Council has not in this agreement made a good faith attempt to protect and improve the investment position of the State Permanent Fund, this Office holds that the entering into the agreement proposed was a legal act well within the Council's power and does not amount to an arbitrary and capricious act.

4. The next question presented is whether the Council in investing under this plan would be guilty of a violation of its duties as trustee for certain trust funds by intermingling the various trust funds for investment. The question is equally applicable to almost all investments made by the Council.

The objection is made on two grounds. The first objection is that such an investment violates Section 10 of the Enabling Act of New Mexico which required that a separate fund and a separate accounting be established for each of the grants under that enactment. 36 Stat. 564. This contention is without merit since Congress in 1957 specifically deleted the seventh paragraph of Section 10 of said Enabling Act, which paragraph contained the requirement that the funds be kept segregated. 71 Stats. 457. Article XII, Section 7 of the Constitution of New Mexico was amended in 1958 and voted on by the people and duly passed to bring our Constitution into conformity with this Enabling Act amendment. Removing that objection, we are left with the problem of whether a trustee can combine trust funds with other funds for investment generally.

While there is admittedly a split of authority on the question, the weight of authority and the better reasoned view is to the effect that the mere combining of funds from several

trusts for investment does not violate the intermingling rule. This is stated by the Restatement of Trusts, Volume 1, at page 650, as follows:

"The mere fact that trust funds are combined with funds not held in trust or with funds of other trusts in making investments does not necessarily make the investment improper, provided that the investments are in other respects proper."

See also in this connection **First National Bank v. Basham,** 238 Ala. 500, 191 So. 873, 125 A.L.R. 656; **Finley v. Exchange Trust Co.,** 183 Okla. 167, 80 P. 2d 296; **Lima First American Trust Co. et al v. Graham et al.,** 54 Ohio App. 85, 6 N.W. 2d 33.

We find, therefore, no violation of the rule against intermingling under the plan proposed.

5. The last and final question presented is whether the agreement is a legal contractual agreement.

This office has already considered this matter and held the agreement to be a valid contractual agreement. We here reaffirm that belief. We do not pass upon the propriety of the contents of the contract nor do we express our view as to whether the agreement is beneficial or detrimental to the interests of the State of New Mexico. Such decisions are within the sole province of the Council. Suffice it to say that the contract was consummated by an offer and an acceptance and is supported by sufficient legal consideration.

Having passed upon each of the questions involved, we are of the opinion that the proposed securities exchange contains no legal impediments.

By: Boston E. Witt

Assistant Attorney General