

(2) *Comparison of Investment Executive Trust of New Zealand, Ltd., with British Type.*

A comparison of the constitution and policy of the Investment Executive Trust of New Zealand, Ltd., which exemplifies the contractual type of trust, with the British type, will serve to reveal the structural weaknesses which have made possible (or at least facilitated and encouraged) the dangerous and objectionable practices referred to in greater detail in Parts III and IV of this report.

(a) *Capital Composition*—The capital resources of investment trusts are procured by means of ordinary shares, preference shares, and debentures. The ordinary rule in trusts of the British type is that at no time should the debenture capital exceed the share capital. The total capital of sixty-three such trusts is distributed as follows:—

Ordinary shares ..	£34,550,000
Preference shares	£36,334,000
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Total share capital ..	£70,884,000
Total debenture capital ..	£45,192,000

From this it will be seen that, in practice, the debenture liability is substantially less than the total share capital.

The capital composition of the Investment Executive Trust of New Zealand, Ltd., is in marked contrast with British practice. The nominal capital is £100,000, but prospectuses so far issued provide for debentures totalling £4,000,000. The total nominal capital is *one-fortieth* of the total nominal value of debentures which may be issued. Paid-up share capital as at 17th October, 1933, totalled approximately £30,000 (ordinary £24,000, preference £5,675), but the debenture issue totalled £493,290, or *over sixteen times* the share capital. Of the ordinary capital of £24,400, two individuals, Messrs. J. W. S. McArthur and C. G. Alcorn, hold £22,575. The control of debenture funds totalling nearly £500,000 is in their hands. In the same way, other contractual trusts operating in New Zealand show a small ratio of share capital to debenture liability.

(b) *Security*.—In the case of trusts of the British type, the security to debenture-holders consists of the total assets of the undertaking. The debenture capital is backed by the whole of the paid-up share capital of the company, and this is normally in excess of the debenture capital. The debenture carries a fixed rate of interest and is a mortgage secured against the whole of the assets of the trust.

The debenture of the Investment Executive Trust of New Zealand, Ltd., is a contract to pay over a certain proportion of the net revenue proceeds derived from the investments made with the debenture funds. These appear to be reduced, before investment, by capital charges in respect of brokerage and administration costs which have totalled up to 10 per cent. of the nominal value of the debentures. Debenture-holders may require repayment of their debentures if the average interest over any two successive years falls below 3 per cent. per annum, or on winding-up of the company; but the assets of the company are not charged by the debentures of any series. The share capital of the company is free from liability in respect of debentures. Hence, the security behind debentures in any series consists simply in the securities and funds held to the credit of the series, and arising from transactions with the funds provided by debenture-holders themselves.

A further essential difference having relation to the question of security is the appointment of trustees. Many, if not all, British trusts appoint trustees with power to inspect security portfolios and power of audit. While the power of trustees will be circumscribed by the conditions of the trust deed, their appointment does provide an additional safeguard against abuse. The Investment Executive Trust of New Zealand, Ltd., appoints no trustee, and debenture-holders have no powers of audit.

The essential bearing of the above on the facts which are disclosed in Parts III and IV of our report is this: By the provision of a small share capital, a small group of individuals has obtained control over a large volume of funds and used