LEGAL LISTS IN TRUST INVESTMENT

INVESTMENT duties of fiduciaries and standards defining their proper conduct in the disposition of billions of dollars now in trust accounts[1] are periodically subjected to intensive examination.[2] Recurring periods of financial depression provide the impetus for a host of surcharge suits by disappointed beneficiaries. Investment policies and practices, seldom questioned in periods of financial stability, are attacked as the primary cause for enormous losses incurred.[3] Attempts thus to shift responsibility for market collapse and to recoup losses from an already harassed trustee were a common phenomenon of trust administration during the severe economic fluctuations of the last decade.

Although not deemed an insurer or guarantor, the trustee has traditionally been expected to exercise a high degree of prudence and diligence in both the selection and supervision of trust investments.[4] Ideal trust administration presupposes the production of an adequate yield for the income beneficiary, as well as preservation of the corpus of the trust estate.[5] Although the distinction between prudence and improvidence in the investment market is often obscure, the trustee is obliged at his peril to discover that distinction, and courts, often less qualified as investment experts, constantly assume to do so. In recognition of the problems thus confronting the trustee, and to provide some security from the ever-present danger of surcharge, courts and legislatures early attempted a more definitive classification of permissible trust investments in what were generally known as "legal lists."[6]

1. There is a paucity of data on the aggregate amount of trust property being administered, but conservative estimates place the total in the billions. Riddle, *Trust Investments: Their Extent and Some Related Economic Problems* (1938) 5 LAW & CONTEMP. PROB. 339.

2. Margraf, *Laws Relating to the Investment of Trust Funds* (1938) 5 LAW & CONTEMP. PROB. 399.

3. Woodruff, *Legal and Investment Standards of Trustees* (1935) 4 FORD. L. REV. 391.

4. See Mann v. Rudder, 225 Ala. 540, 144 So. 13 (1932); Tannenbaum v. Sea Coast Trust Co., 16 N. J. Misc. 234, 198 Atl. 855 (Ch. 1938). See generally Hardsall, *Conflict of Interest When a Trustee Invests Trust Funds* (1936) 14 CHI. KENT L. REV. 329; Wright, *The Measure of the Trustee's Liability For Improper Investments* (1932) 80 U. OF PA. L. REV. 1105; 2 SCOTT ON TRUSTS (1939) §§227-231; 3 BOGERT, TRUSTS AND TRUSTEES (1935) §§ 611-612.

5. See Matter of Hurlbut, 210 App. Div. 456, 206 N. Y. Supp. 448 (2d Dep't 1924); LORING, A TRUSTEE'S HANDBOOK (4th ed. 1928) 132-153. Idealism, however, must succumb to the unpredictable fluctuations of the investment market for which trustees normally are not held accountable. See *In re* Flint's Will, 240 App. Div. 217, 269 N. Y. Supp. 470 (2d Dep't 1934) ("The law does not exact prescience of a trustee."); Wright, *The Measure of the Trustee's Liability For Improper Investments* (1932) 80 U. OF PA. L. REV. 1105.

6. See Freifield, *Investment of Trust Funds* (1931) 5 U. OF CINN. L. REV. 1. But *cf.* Robinson, *Trustee's Investments In Massachusetts* (1934) 14 B. U. L. REV. 88.

I.

English courts of equity adopted the rule that the trustee should confine his investments to government securities and bank annuities if he would secure himself from liability for prospective losses.[7] Mortgages, industrial stocks and bonds and all other loans on personal or other security were apparently deemed inherently speculative and therefore prohibited unless specifically authorized by the settlor.[8] Statutory action soon extended the permitted fields within which the trustee might safely invest,[9] and thereby alleviated the full rigor of this restrictive judicial definition of prudence.

With sound government securities at a premium in the early history of this country,[10] it is not surprising that early American courts refused to follow the English practice.[11] All states imposed the basic requirements of prudence, good faith and the exercise of a sound discretion on the part of the fiduciary in selecting trust investments, but two divergent lines of authority early characterized the definition of prudence in this regard. Massachusetts, and courts adopting the so-called Massachusetts rule,[12] refused to attempt any classification of particular types of securities to be deemed permissible. All investments of whatever nature were to be solely subjected to the loose, uncertain and extremely flexible standard of prudence.[13] Mortgages, government bonds, industrial securities and any other investments regarded by the reasonable, prudent man as sound, and without the stigma of dangerous speculation, were regularly approved.[14] Results in individual instances were thus rendered entirely unpredictable, but both courts and trustees were at the same time unhampered in the exercise of their discretion by any previous

7. *Ex parte* Cathorpe, 1 Cox. Eq. Cas. 181 (Ch. 1785); Raby v. Ridehalgh, 7 De G. M. & G. 104 (Ch. 1855). Note (1921) 69 U. OF PA. L. REV. 189; 2 SCOTT ON TRUSTS (1939) § 227.4.

8. English cases omit discussion of the reasons for excluding other securities but it has been suggested that the desire to create a market for government securities was a compelling factor. SCOTT, *op. cit. supra* note 4, § 227.4. See White and Lawres, *The Modernization of Legal Lists* (1938) 5 LAW & CONTEMP. PROB. 386, 387, n. 3.

9. For recent thorough classification, see TRUSTEE'S ACT, 1925, 15 Geo. V. c. 19, §§ 1-11. BOGERT, *op. cit. supra* note 4, § 163.

10. See SCOTT, *op. cit. supra* note 4, § 227.5.

11. Harvard College v. Amory, 9 Pick. 446 (Mass. 1830); King v. Talbot, 40 N. Y. 76 (1869). See SCOTT, *op. cit. supra* note 4, § 227.5.

12. "All that can be required of a trustee to invest, is, that he shall conduct himself faithfully and exercise a sound discretion. He is to observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested." Putnam, J., in Harvard College v. Amory, 9 Pick. 446, 461 (Mass. 1830). See also *In re* Banning, 9 Hawaii 453 (1894); Robinson, *Trustee's Investments In Massachusetts* (1934) 14 B. U. L. REV. 88.

13. See Appeal of Dickinson, 152 Mass. 184, 25 N. E. 99 (1890); *In re* Buhl's Est., 211 Mich. 124, 178 N. W. 651 (1920).

14. See Brown v. Brown, 22 Hawaii 715 (1915); Robinson, *supra* note 12.

definitive classification. Surcharges against the diligent trustee were seldom imposed, but the rule presented no obstacle for directly contrary results on identical investment policies should the court be unfavorably impressed with any particular action or investment by a fiduciary.[15] In the absence of statutory modification, this rule remains the sole guide and standard for the trustee in those jurisdictions at the present time.[16]

Under precisely the same flexible rule of prudence, the New York courts, on the other hand, seriously restricted the scope of the trustee's discretion.[17] Acknowledging the liberality of the Massachusetts courts, the Court of Appeals, nevertheless, early declared that all industrial stocks and bonds were imprudent, speculative investments for fiduciaries.[18] Unless specifically authorized by the settlor, the trustee who invested in such securities was forced to assume the risk of any depreciation from whatever cause. General discretionary powers in the trust instrument did not authorize such so-called speculation with the trust corpus.[19] The "legal list" in states adopting this rationale was thereby virtually confined to mortgages, corporate bonds secured by mortgage and government securities. In the absence of specific statutory or settlor authorization, many jurisdictions regularly surcharge fiduciaries for depletion resulting from investment in unsecured corporate issues.[20]

Neither rule of the early American common law was entirely satisfactory. In the hands of an experienced trustee, the Massachusetts rule was undoubtedly superior, since it offered a wider latitude and opportunity to use skill

15. Compare Appeal of Dickinson, 152 Mass. 184, 25 N. E. 99 (1890), with First Nat. Bank of Boston v. Truesdale Hospital, 288 Mass. 35, 192 N. E. 150 (1934), 48 HARV. L. REV. 347. See also Creed v. McAleer, 275 Mass. 353, 175 N. E. 761 (1931), 65 U. S. L. REV. 570.

16. See Old Colony Trust Co. v. Comstock, 290 Mass. 377, 195 N. E. 389 (1935); Springfield Safe Deposit & Trust Co. v. First Unitarian Soc. *et al.*, 293 Mass. 480, 200 N. E. 541 (1936); Roberts v. Michigan Trust Co., 273 Mich. 91, 262 N. W. 744 (1935). See (1930) 50 TRUST CO. 427.

17. King v. Talbot, 40 N. Y. 76 (1869).

18. *Ibid.*

19. The settlor had authorized the trustee to exercise "full discretion as to the investment of my estate . . ." *Id.* at 87. But *cf. In re* Leonard's Will, 118 Misc. 598, 193 N. Y. Supp. 916 (Surr. Ct. 1922). See (1926) 26 COL. L. REV. 453.

20. Sellers v. Milford, 101 Ind. App. 590, 198 N. E. 456 (1935); Marshall v. Braucher, 159 Ore. 491, 80 P. (2d) 42 (1938). But see *In re* Wood's Est., 130 Pa. Super. 397, 197 Atl. 638 (1938); Carwithen's Est., 28 D. & C. 66 (Pa. 1937). Notes (1938) 86 U. OF PA. L. REV. 791; (1937) 85 U. OF PA. L. REV. 647.

Constitutional provisions in four states forbid legislative authorizations of corporate stocks as permissible trust investments. ALA. CONST. §74; COLO. CONST. Art. V, §36; MONT. CONST. Art. V, §37; WYO. CONST. Art. III, §38. Pennsylvania recently repealed a similar provision. PA. CONST. Art. III, §22, as amended, ACTS AND VETOES (Spec. Sess. 1933-1934) app. 338. For the effect of such constitutional limitations upon the trustee's discretion, see Sims v. Russell, 236 Ala. 562, 183 So. 862 (1938); *In re* Maroney's Est., 311 Pa. 336, 166 Atl. 914 (1933).

and ability in the investment market to greater advantage.[21] Cognizant of the fact, however, that all fiduciaries are not investment experts, the New York courts sacrificed desirable flexibility in favor of certainty and better protection for the estates managed by less competent trustees.[22] Both, also, were founded solely upon judicial pronouncement, and soon resulted in "legal lists" by judicial stare decisis — at most a rather unpredictable guide for the trustee. As a consequence he was often surcharged under circumstances varying but slightly from the case law upon which he relied.[23]

In view of such uncertainty, and to alleviate the uncompromising rigidity of the New York rule, legislative action in many states became imperative. Unprecedented increases in the number and size of trust funds and the specialized requirements of savings banks and insurance companies resulted in a demand for sound securities far in excess of the available supply.[24] Statutory action usually took the form of prescribed eligibility tests for the several types of investments thereby made available and permissible for the trustee, rather than any definitive listing of particular securities within each class.[25] Mortgages, government bonds of federal, state and local origin, public utility and railroad issues typified the usually permitted groups.[26] The tests prescribed were designed to indicate generally the accepted characteristics of the "good" investments in each category and to exclude unworthier ones. The appellation "legal list" as pertaining to such statutory specification is therefore largely a misnomer. All securities or particular issues conforming to the requirements are, however, loosely described as "legals," as distinguished from "nonlegals" of the same or unpermitted classes failing to meet the specifications imposed. The duty of determining whether a particular

21. LORING, *op. cit. supra* note 5, at 140; (1929) 48 TRUST CO. 413. Discretionary powers were not unlimited, however. Appeal of Dickinson, 152 Mass. 184, 25 N. E. 99 (1890) (surcharge for failure to diversify investments); Stewart v. National Shawmont Bank, 69 F. (2d) 694 (C. C. A. 1st, 1934), 34 COL. L. REV. 1564 (negligent supervision); Michigan Home Soc. v. Corning, 164 Mich. 395, 129 N. W. 686 (1911) (unsecured personal note); Sims v. Russell, 236 Ala. 562, 183 So. 862 (1938) (failure to promptly collect).

22. See Simmons v. Oliver, 74 Wis. 633, 43 N. W. 561 (1889). Perry suggested that with the increase in available government bonds the trend should be towards the strict English rule. PERRY, TRUSTS AND TRUSTEES (6th ed. 1911) § 456. See Indiana Trust Co. v. Griffith, 176 Ind. 643, 95 N. E. 573 (1911).

23. Compare Appeal of Dickinson, 152 Mass. 184, 25 N. E. 99 (1890), with Creed v. McAleer, 275 Mass. 353, 175 N. E. 761. See SCOTT, *op. cit. supra* note 4, § 227.

24. Matter of Hammersley's Est., 152 Misc. 903, 274 N. Y. Supp. 303 (Surr. Ct. 1934); REP. N. Y. SUPT. OF BANKS (1901) 5, 31; White and Lawres, *The Modernization of Legal Lists* (1938) 5 LAW & CONTEMP. PROB. 386, 388 n. 7.

25. For a complete collection of all statutes, see 3 BOGERT, TRUSTS AND TRUSTEES (2d ed. 1935) §§ 616-663; MCKINNEY, TRUST INVESTMENTS (2d ed. 1927). For recent amendments, see Margraf, *Laws Relating to Investment of Trust Funds* (1938) 5 LAW & CONTEMP. PROB. 399.

26. See, *e.g.*, N. Y. DEC. EST. LAW § 111; N. Y. BANK. LAW § 235; CONN. GEN. STAT. (1930) § 4836.

mortgage, stock or municipal bond, for instance, conforms to the requirements of the so-called "list" is imposed solely upon the trustee and few statutes attempt to relieve him of this responsibility.[27]

The range of securities allowed and the types of specifications imposed by the legislatures of particular states are as variable as at common law.[28] As might be expected, views on the success or failure of the legislative enactments were highly divergent.[29] Nevertheless, such legislative action did promote certainty for the bewildered trustee and provided an element of protection for both the beneficiary and fiduciary. The trustee was provided with a wider field within which he might invest with relative security, and, at the same time, it was rendered less likely that he would ignore the permitted group in favor of more speculative securities not receiving legislative approbation.[30] Such statutes do not, however, entirely absolve the trustee from the duty of exercising reasonable care and prudence in selecting particular investments within the legal lists.[31] Proof of negligence or gross abuse of discretion in particular circumstances will still result in liability for losses whether the investment is in legal or non-legal securities.[32] Practically, however, courts are reluctant to impose such liability in the face of a legislative stamp of approval.[33] This factor has often led to severe criticism of all such

27. But see *In re* Stupack, 274 N. Y. 198, 8 N. E. (2d) 485 (1937); Mills v. Bluestein, 275 N. Y. 317, 9 N. E. (2d) 944 (1937), *rev'g*, 250 App. Div. 440, 294 N. Y. Supp. 186 (2d Dep't 1937).

28. See McKINNEY, *op. cit. supra* note 25, at xii, condemning lack of uniformity in statutes. But *cf.* Scott, *Responsibility of A Trustee With Regard to Original Investments* (1931) 52 TRUST Co. 181, expressing opposition to a proposed Uniform Trust Law.

For discussion of local statutes and problems, see Freifield, *Investments By Fiduciaries Under the New Ohio Probate Code* (1931) 5 U. OF CINN. L. REV. 429; Whitaker, *The Problem of Legal Investments For Trust Funds* (1934) 8 TEMP. L. Q. 473 (Penn.); Markham, *Trust Investments in North Carolina* (1935) 14 N. C. L. REV. 160; Olsin and Brandschaft, *Problems of Trust Administration In New Jersey* (1935) 4 MERCER BEASLEY L. REV. 31; Grimm, *Legal Investment For Trust Funds in Missouri* (1929) 14 ST. LOUIS L. REV. 277; Comment (1936) 84 U. OF PA. L. REV. 640; Legis. (1934) 19 IOWA L. REV. 354 (Ohio, Fla. and Iowa); Note (1929) 4 TEMP. L. Q. 57 (N. J. and Penn.).

29. See Woodruff, *Legal and Investment Standards of Trustees* (1935) 4 FORD. L. REV. 391; Edwards, *New Standards For Railroad Securities* (1937) 64 TRUST Co. 174.

30. Legis. (1936) 49 HARV. L. REV. 821.

31. SCOTT, *op. cit. supra* note 4, § 227.12; RESTATEMENT, TRUSTS § 227, comment *p*.

32. *In re* Young's Est., 249 App. Div. 495, 293 N. Y. Supp. 97 (2d Dep't 1937), *rev'g*, 159 Misc. 611, 288 N. Y. Supp. 569 (Surr. Ct. 1936) (lax supervision of mortgage); *In re* Dalsimer's Will, 251 App. Div. 385, 296 N. Y. Supp. 209 (1st Dep't 1937), *aff'g*, 160 Misc. 906, 291 N. Y. Supp. 34 (Surr. Ct. 1936) (improper investigation of mortgage security); *In re* Blake's Will, 146 Misc. 780, 263 N. Y. Supp. 310 (Surr. Ct. 1933) (participation mortgage maturing long after termination of trust).

33. See Matter of Flint, 240 App. Div. 217, 269 N. Y. Supp. 470 (2d Dep't 1934), *rev'g*, 148 Misc. 474, 266 N. Y. Supp. 392 (Surr. Ct. 1933), 33 COL. L. REV. 1270; *In re* Froelich's Est., 150 Misc. 371, 269 N. Y. Supp. 541 (Surr. Ct. 1934); *In re* Frazer's Est., 150 Misc. 43, 268 N. Y. Supp. 477 (Surr. Ct. 1933). But *cf. In re* Blake's Will, 146 Misc. 780, 263 N. Y. Supp. 310 (Surr. Ct. 1933).

statutes as unwarranted legislative assumption of fiduciary responsibility.[34] In view of the previous dilemma presented to the diligent trustee, and the added factor that the individual settlor may freely direct or permit circumvention of the legislative standards imposed,[35] the criticism would seem largely unwarranted.

Unfortunately the courts are still in confusion on the effect of such statutes upon the trustee's discretion to select investments not within the protected category. Results are made to depend upon the often fortuitous choice of words selected by the legislature in establishing the protected lists. No clear definition or method of ascertaining the difference between a "mandatory" statute and a "permissive" or "directory" statute has been formulated. Yet the important question of the liability of a fiduciary investing in non-legal securities is made to depend upon such illusory distinctions.[36]

Statutes held to be mandatory are said to prohibit absolutely any deviation from the prescribed lists[37] without specific authority from the court or settlor

34. See White and Lawres, *supra* note 24, at 397. Many statutes expressly relieve the trustee from liability for losses incurred in legals. See, *e.g.*, W. VA. CODE ANN. (Michie, 1937) § 4216.

35. All statutory authorization or restriction is either expressly or by judicial construction made subject to any contrary provision of the trust instrument. Wilmington Trust Co. v. Worth, 19 Del. Ch. 314, 167 Atl. 848 (1933); Shinn, *Exoneration Clauses In Trust Instruments* (1933) 42 YALE L. J. 359.

(a) Specific directions by testator may render statutory legals non-legal for purposes of surcharge: Gaines v. Arkansas Nat. Bank, 170 Ark. 679, 280 S. W. 993 (1926); *In re* Shaw's Est., 122 N. J. Eq. 536, 195 Atl. 525 (1937). But *cf. In re* London's Est., 104 Misc. 372, 171 N. Y. Supp. 981 (Surr. Ct. 1918), 32 HARV. L. REV. 181.

(b) General discretionary powers usually are construed as authorizing non-legal investments if prudent. Falls v. Carruthers, 20 Tenn. App. 681, 103 S. W. (2d) 605 (1936); Willis v. Braucher, 79 Ohio St. 290, 87 N. E. 185 (1909), (1938) 15 TENN. L. REV. 169. A common interpretation, however, restricts the trustee in the exercise of such discretion to the statutory list. As such, the clauses are, of course, illusory. Equitable Trust Co. v. Snader, 20 Del. Ch. 278, 174 Atl. 132 (1934). *Cf. In re* Harbeck's Est., 142 Misc. 57, 254 N. Y. Supp. 312 (Surr. Ct. 1931).

(c) The word "securities" usually receives a broad interpretation authorizing common stocks and other non-legal investments. City Bank Farmer's Trust Co. v. Lewis, 122 Conn. 384, 189 Atl. 178 (1937); RESTATEMENT, TRUSTS § 227, comment *u*. But see Davis v. Davis Trust Co., 106 W. Va. 228, 145 S. E. 588 (1928).

36. See Legis. (1936) 49 HARV. L. REV. 821; SCOTT, *op. cit. supra* note 4, § 227.13. That "may invest" may be interpreted as "shall invest" and be exclusive and therefore mandatory, see *In re* Jones' Will, 202 Minn. 187, 277 N. W. 899 (1938); *In re* Vanderlip's Will, 202 Minn. 206, 277 N. W. 909 (1938), 22 MINN. L. REV. 1070. That "shall invest" may mean "may invest" only, and therefore not be mandatory, see *In re* Michaelson, 162 Misc. 847, 296 N. Y. Supp. 119 (Sup. Ct. 1937), interpreting N. Y. CIV. PRAC. ACT § 1384-1 regarding guardian's investment.

37. For examples of mandatory statutes, see LA. GEN. STAT. ANN. (Dart, 1939) § 9850.62 ("trustee shall invest . . . only in . . ."); FLA. COMP. GEN. LAWS (1927) § 6127 ("may invest . . . only in."). Trust companies are most frequently so limited. HAWAII REV. LAWS (1935) § 6909 ("shall be made only in . . ."); IDAHO CODE ANN.

to do so. They usually purport, expressly or by implication, to establish the only available securities for the fiduciary. Other mandatory statutes permit a trustee to go beyond the prescribed list provided he obtain prior court authorization.[38] Whenever such positive statutory prescription is imposed, investments in securities other than those specified are at the sole risk of the trustee.[39] Failure to conform with the statutory mandate constitutes a breach of trust and the violator automatically becomes liable for all losses from whatever cause,[40] regardless of the actual value of the security as an investment or the amount of prudence involved. Thus, where prior court authorization is specifically required, it has been held that courts are powerless later to ratify investments previously made in an effort to absolve the unwary fiduciary from liability.[41] Also, where the list for guardians purports to be exclusive, investments in other securities, even if deemed proper for other trustees, are unauthorized.[42] Statutory specification of this character thus completely supplants the discretionary powers of the fiduciary at common law. The quest for the prudent investment becomes mired in a maze of technicalities and the trustee's liability determined without reference to prudent conduct. The criticism generally leveled at such complete legislative assumption of fiduciary discretion may therefore be well-founded.[43] However, again, it is not the policy of such statutes that the mandates so established shall be so supremely

(1932) § 25-1502 ("trust companies may invest in . . . only."). IND. STAT. ANN. (Burns, 1933) § 18-1204 ("shall invest . . . but no others . . .").

Statutes governing savings banks, insurance companies and fiduciaries such as guardians and court custodians of funds are usually mandatory. See N. Y. BANK. LAW § 235; N. Y. CIV. PRAC. ACT § 1384-1; ILL. STAT. ANN. (Smith-Hurd, 1936) c. 64 § 22.

38. See note 37 *supra*, and GA. CODE (1933) § 108-417 ("any other investments . . . shall be made under an order of court . . . or else at the risk of the trustee . . ."); IOWA CODE (1935) § 12772 ("all . . . investments . . . shall first be reported to the court . . .").

39. *In re* Nolan's Guardian, 216 Iowa 903, 249 N. W. 648 (1933) (subsequent court approval of no avail when prior authorization required); *In re* Jefferson's Est., 219 Iowa 429, 257 N. W. 783 (1934) (depressions and not poor investment responsible for loss deemed irrelevant).

40. Home Savings & Loan Co. v. Strain, 130 Ohio St. 53, 196 N. E. 770 (1935). But *cf.* People's State Bank & Trust Co. v. Wade, 269 Ky. 89, 106 S. W. (2d) 74 (1937).

41. Chapman v. American Surety Co., 261 Ill. 594, 104 N. E. 247 (1914); *In re* Lalla's Est., 362 Ill. 621, 1 N. E. (2d) 50 (1936); Brewer v. Herron, 171 Miss. 435, 157 So. 522 (1934). Court approval or "ratification" generally, however, protects the trustee in the absence of subsequent neglect in supervising the investment. Johnson v. Johnson, 168 Md. 568, 179 Atl. 831 (1935); *In re* Lawson's Est., 215 Iowa 752, 244 N. W. 739 (1932). But the trustee must present all known changes affecting the investment thereafter to the court, and for failure to do so will be surcharged despite court's prior approval. Zimmerman v. Coblentz, 170 Md. 468, 185 Atl. 342 (1936). But *cf. In re* Paulsen's Guardian, 229 Wis. 262, 282 N. W. 36 (1938).

42. *In re* Farina, 253 App. Div. 510, 2 N. Y. S. (2d) 987 (2d Dep't 1939). The New York guardian statute omitted reference to guaranteed mortgage certificates allowed by N. Y. DEC. EST. LAW § 111 at that time.

43. See note 34 *supra*.

authoritative that the creator of the trust shall be excluded from the right to select any investment standards or powers he may desire for the guidance of his trustee.[44] Despite the often stated requirements that authority to exceed the bounds of such rigorous statutory limitations must be clearly shown,[45] courts anxious to protect the innocent trustee have been astute in implying such powers from the trust instrument.[46].

The second type of statutory specification, and by far the more usual, is the so-called permissive statute. Usually expressed in such terms as "the trustee may invest"[47] or "it shall be lawful to invest,"[48] followed by the types of securities deemed permissible, such statutes are said to create a "protective haven"[49] for the trustee and a strong presumption of good faith and sound discretion for any investments selected from the favored category.[50] Unlike the mandatory statute, however, securities not included therein are not automatically excluded from the trustee's proper consideration.[51] Automatic liability for any losses suffered in any non-legal security does not follow. The trustee may not, of course, rely upon legislative approval as protection from attack, but proof of due care and prudence as required under the Massachusetts rule may justify deviations from the permitted lists and not render the trustee an insurer.[52] Legislative omnipotence in specifying sound investment criteria does not purport to be exclusive or authoritatively supreme. In fact, periods of economic fluctuations may render large portions of the traditionally approved securities unwise for trust investment.[53] Exculpatory clauses and other authorization in the trust instrument to exceed the permis-

44. See note 35 *supra*. Wilmington Trust Co. v. Worth, 19 Del. Ch. 314, 167 Atl. 848 (1933).

45. Equitable Trust Co. v. Snader, 20 Del. Ch. 278, 174 Atl. 132 (1934); Gould v. Gould, 126 Misc. 54, 213 N. Y. Supp. 286 (Sup. Ct. 1925), (1926) 26 COL. L. REV. 453.

46. New York courts have been particularly lenient in this respect. *In re* Leonard's Will, 118 Misc. 598, 193 N. Y. Supp. 916 (Surr. Ct. 1922); But *cf. In re* Robbin's Will, 135 Misc. 220, 237 N. Y. Supp. 409 (Surr. Ct. 1929); *In re* Harbeck's Est., 142 Misc. 57, 254 N. Y. Supp. 312 (Surr. Ct. 1931).

47. *E.g.*, ALA. CODE ANN. (Michie, 1928) § 10,417(1); N. J. REV. STAT. (1937) § 3:16-1.

48. *E.g.*, ARK. DIG. STAT. (Pope, 1937) § 6258 (a); COLO. STAT. ANN. (Michie, 1935) c. 176, § 122.

49. See *In re* Cook's Est., 20 Del. Ch. 123, 171 Atl. 730 (1934); *In re* Gibson's Est., 312 Pa. 359, 167 Atl. 282 (1933).

50. Clark v. Beers, 61 Conn. 87, 23 Atl. 717 (1891). The presumption is rebutted by proof of negligence or lack or due care. *In re* Hall, 164 N. Y. 196, 58 N. E. 11 (1900).

51. See cases cited *supra* note 50; Mann v. Rudder, 225 Ala. 540, 144 So. 13 (1932); *In re* Cook's Est., 20 Del. Ch. 123, 171 Atl. 730 (1934).

52. See cases cited *supra* notes 50 and 51.

53. See note 97 *infra;* Morris Community Chest v. Wilentz, 124 N. J. Eq. 580, 3 A. (2d) 808 (1939) (court authorizing application to buy common stocks because of low yields in legals); *In re* Mallon, Ill. Prob. Ct., June 20, 1935 (petition of guardian to buy U. S. Bonds denied because too low yield). But *cf. In re* Muller's Will, 155 Misc. 748, 280 N. Y. Supp. 345 (Surr. Ct. 1935) (petition to exceed legal list denied).

sive list at will are of relatively less importance under this type of legislative specification. Their only function would seem to be to relieve the trustee of the burden of proof on the issues of prudence[54] and specific authority or direction to invest in certain non-legals may constitute a defense for the trustee in most instances.[55]

A third limitation upon the trustee's discretion to select securities other than those receiving legislative approval arises in a few states from a narrow construction of the permissive statute in the light of previous judicial restrictions. In New York, Wisconsin and other states originally adopting the New York rule at common law, mortgages and government bonds constituted the only investments permitted for trust accounts. Subsequent statutory modification and extension of the permitted fields was therefore deemed by the courts to constitute the maximum limit for proper disposition of trust funds.[56] Despite the fact that the words of the statute were permissive only,[57] and did not purport to be exclusive or establish an absolute limit upon the trustee's discretion, they were judicially construed as mandatory, and failure to conform to the legislative requirements constituted a breach of trust as a matter of law.[58] As in the case of the mandatory statute, such a breach of trust could not be justified by any amount of proof of prudence or the actual investment value of the security. Actually, all cases first enunciating this doctrine were dealing with investment conduct which would be imprudent under any rule or statute,[59] and the argument advanced served only as a bolstering effect for an otherwise justified surcharge. Thus, speculation in marginal accounts on the security exchanges in non-legal stocks and bonds was early condemned as a "devastavit" for exceeding the statutory qualifications.[60] Such speculation with trust funds, however, whether the securities involved were legal or non-legal for investment purposes, would constitute

54. See City Bank Farmer's Trust Co. v. Lewis, 122 Conn. 384, 189 Atl. 179 (1937); Guaranty Trust Co. v. Fisk, 244 App. Div. 200, 278 N. Y. Supp. 809 (1st Dep't 1935).

55. *In re* Allis' Est., 191 Wis. 23, 209 N. W. 945 (1926); *In re* Robinson's Est., 155 Misc. 855, 280 N. Y. Supp. 687 (Surr. Ct. 1935). A trustee may be enjoined from speculating. Carrier v. Carrier, 226 N. Y. 114, 123 N. E. 135 (1919).

56. *In re* Hamersley's Est., 152 Misc. 903, 274 N. Y. Supp. 303 (Surr. Ct. 1934); Wotton v. DeReau, 59 App. Div. 584, 69 N. Y. Supp. 753 (1st Dep't 1901).

57. *E.g.*, N. Y. DEC. EST. LAW § 111—"the trustee may invest . . ." The list for savings banks is made available by reference to N. Y. BANK. LAW § 235 and as to such institutions the list purports to be exclusive—*i.e.*, ". . . and no others . . ." No such limitation is made in reference to other fiduciaries, however. But see dissenting opinion of O'Brien, J., in Delafield v. Barret, 270 N. Y. 43, 200 N. E. 67 (1936).

58. *In re* Fouck's Est., 213 Wis. 550, 252 N. W. 160 (1934); *In re* Allen's Est., 218 Wis. 349, 259 N. W. 848 (1935).

59. Steele v. Leopold, 135 App. Div. 247, 120 N. Y. Supp. 569 (1st Dep't 1909). See cases cited *infra* notes 60 and 61.

60. National Surety Co. v. Manhattan Mfg. Co., 185 App. Div. 733, 174 N. Y. Supp. 9 (1st Dep't 1919).

a breach of trust regardless of the investment powers of the fiduciary.[61] The proper reason for surcharge was not the act of investing in non-legal securities alone, but rather, speculation in its most obvious form. The doctrine thus founded upon obiter, has, nevertheless, been retained, and succeeding cases which have regularly announced it as a major premise, have been seldom questioned.[62] The doctrine presupposes a rigid adherence by the New York courts to century-old judicial pronouncement of what constituted prudence in the disposition of trust funds.[63]

Indicative that future cases may correct the strained construction involved, recent pronouncements of the New York courts have prepared the way for total emasculation of this false premise. In *Delafield v. Barrett,*[64] investment in non-legals was relegated to the status of a "mere devastavit" involving liability for losses as required by "public policy," but not in fact a "breach of trust" or in any way "tortious."[65] In subsequent cases the lower courts have openly challenged the validity of prior dicta and holdings imposing the liability of an insurer upon the prudent trustee for investments exceeding the specifications of the statutory list.[66] The Court of Appeals has not as yet, however, found it necessary to clarify the confused situation or elucidate more fully upon the supposed "public policy" involved. In *Stark v. National*

61. See *In re* Cady's Est., 211 App. Div. 373, 207 N. Y. Supp. 385 (4th Dep't 1925); *In re* Hall, 164 N. Y. 196, 58 N. E. 11 (1900); United States Nat. Bank & Trust Co. v. Sullivan, 69 F. (2d) 412 (C. C. A. 7th, 1934).

62. See *In re* Muller's Will, 155 Misc. 748, 280 N. Y. Supp. 345 (Surr. Ct. 1935); *In re* Doelger's Est., 254 App. Div. 178, 4 N. Y. S. (2d) 334 (1st Dep't 1938), *rev'g,* 164 Misc. 590, 299 N. Y. Supp. 565 (Surr. Ct. 1937); (1939) 39 COL. L. REV. 313.

63. Undoubtedly when first enacted the statute did represent an extension of permitted fields beyond then existing judicial restriction. But certainly judicial opinion upon such elusive conceptions as "the prudent investment" are subject to change and may eventually exceed the legislative liberality, unless legislative specifications are deemed definitive of prudence for all time until themselves amended. No cases present very lucid discussions of the reasoning involved. See cases cited *supra* notes 61 and 62.

64. 270 N. Y. 43, 200 N. E. 67 (1936), (1937) 46 YALE L. J. 1085, (1936) 5 BROOKLYN L. REV. 340, (1936) 22 CORN. L. Q. 147.

65. The appellation given to the condemned investment is extremely flexible. When it makes little difference, it constitutes a "breach of trust." *In re* Fouck's Est., 213 Wis. 550, 252 N. W. 160 (1934). To avoid the necessity of holding the trustee liable for the full value of stolen non legal securities, investment therein was held creative of liability only for "depreciation" but not in fact a "breach of trust." *In re* Darlington's Est., 245 Pa. 212, 91 Atl. 486 (1914). To avoid the doctrine of joint tort feasors denying contribution *inter se,* it was called a "devastavit" but not "breach of trust" or "tortious." Steele v. Leopold, 135 App. Div. 247, 120 N. Y. Supp. 569 (1st Dep't 1909). Here also (and in all subsequent cases) called a "devastavit" to uphold an indemnity contract as not violative of public policy as it well might be if the act were a "breach of trust." For an example of the ultimate confusion thus inspired, see *In re* Burr, 118 App. Div. 482, 104 N. Y. Supp. 29 (3d Dep't 1907).

66. See Mills v. Bluestein, 250 App. Div. 440, 294 N. Y. Supp. 186 (2d Dep't 1937), *rev'd,* 275 N. Y. 317, 9 N. E. (2d) 944 (1937).

City Bank,[67] the opportunity to do so was presented but ignored. A transfer agent participating with the trustee is an "exchange" of one non-legal security for another issue of the same nature was relieved of liability for subsequent depreciation of the investment, on the ground that the "exchange" was prudent.[68] The fact that the new security was not within the protected category was deemed irrelevant. This case represents a definite change of position and cannot be reconciled with prior authority imposing liability upon anyone knowingly participating with a fiduciary investing in unapproved securities.[69] While not purporting to overrule the dicta of the previous cases, it seems clear that New York may soon join the states operating under the usual permissive statute. Liability will be imposed upon the trustee solely for unwarranted administration of the fund and not for technical non-conformity to a permitted standard of conduct.[70]

As a result of the harsh implications flowing from this construction of the New York statute, the New York courts have shown themselves ready to seize upon any indication in the trust instrument to authorize exceeding the narrow bounds of the legal list.[71] This unusual willingness to find authority in ambiguous phraseology[72] would indicate that the alleged "public policy" involved cannot be too deep-rooted. If discretionary investment powers in the trust instrument will relieve the trustee from liability for losses incurred in non-legal, but sound corporate stocks and bonds, then it would seem that courts should be willing to find identical discretionary powers inherent in the trustee's office which would have the same effect.

II.

Closely analogous to the problems of the trustee's liability for non-legal investments are those concerning the retention of such securities in the trust estate.[73] His duties toward non-legals received from the settlor, and his

67. 278 N. Y. 388, 16 N. E. (2d) 376 (1938), *rev'g*, 253 App. Div. 801, 1 N. Y. S. (2d) 738 (1st Dep't 1937).

68. Action which without the implication inherent in the accepted theory would have been an "investment" had to be relegated to the status of an "exchange" to attain the desired result. *Cf.* Mertz v. Guaranty Trust Co., 247 N. Y. 137, 159 N. E. 888 (1928).

69. Steele v. Leopold, 135 App. Div. 247, 120 N. Y. Supp. 569 (1st Dep't 1909); National Surety Co. v. Manhattan Mfg. Co., 185 App. Div. 733, 174 N. Y. Supp. 9 (1st Dep't 1919).

70. See (1937) 47 YALE L. J. 299; (1939) 16 N. Y. U. L. Q. REV. 321.

71. See note 46 *supra*.

72. See SCOTT, *op. cit. supra* note 4, § 227.14; BOGERT, *op. cit. supra* note 4, § 682.

73. See generally Bogert, *The Trustee's Duty With Regard To Conversion of Investments* (1933) 1 U. OF CHI. L. REV. 28; Scott, *Responsibility of A Trustee With Regard To Original Investments* (1931) 52 TRUST CO. 181; (1930) 79 U. OF PA. L. REV. 77; (1932) 30 MICH. L. REV. 815; (1930) 30 COL. L. REV. 1100; SCOTT, *op. cit. supra* note 4, §§ 230-230.2.

duties with regard to his own investments, legal when made but subsequently falling out of the protected category, should be and usually are identical.[74]

Early authority allowed the fiduciary to retain all investments received from the settlor, adopting the rationale that the creator of the trust, in making the investment himself, thereby indicated his belief in the soundness of the security. The trustee in taking over his estate was, therefore, held impliedly authorized to continue the same investment, despite the fact that he might be exceeding the powers of his office were he originally to invest therein.[75] Apart from what would seem to be a non-sequitor involved in such reasoning, the contrary view adopted by the great majority of courts in this country appears much sounder. The fact that the settlor of the trust indulged in speculative enterprises during his own control over the funds involved should not be regarded as an indication of authority in the trustee to continue to endanger the corpus in like manner.[76] Unless the instrument or a statute[77] gives authority to retain, a duty to convert all non-legal investments is therefore usually imposed upon the fiduciary today.[78]

Pronouncements of the duty to sell non-legal securities found in the trust estate have necessarily been couched by the courts in somewhat vague phraseology and usually with the admonition that each case must depend largely upon its own circumstances.[79] General phrases culled from judicial opinions cannot be accepted as sufficiently precise to enable fiduciaries to determine their exact responsibilities. Usual statements of the rules governing such retention are expressed in two theoretically different forms, largely dependent upon the type of statute or rule of court governing original investments by the fiduciary within the particular jurisdiction.[80]

1. The trustee is under a duty to convert all non-legal investments within a reasonable time and invest in legal securities.[81]

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74. See BOGERT, *supra* note 73. For an example of originally non-legal investments becoming legal then followed by loss, see Matter of Adriance, 145 Misc. 345, 260 N. Y. Supp. 173 (Surr. Ct. 1932) (no liability), 32 COL. L. REV. 1446, (1933) 19 VA. L. REV. 630.

75. Matter of Weston, 91 N. Y. 502 (1883); (1930) 30 COL. L. REV. 1166. Compare North Adams Nat. Bank v. Curtis, 278 Mass. 471, 180 N. E. 217 (1932), with *In re* Parson's Est., 143 Misc. 368, 257 N. Y. Supp. 339 (Surr. Ct. 1932).

76. Scott, *Responsibility of a Trustee With Regard To Original Investments* (1931) 52 TRUST CO. 181.

77. Many statutes authorize retention if prudent. See, *e.g.*, CONN. GEN. STAT. (1930) § 4837; DEL. REV. CODE (1935) § 4401; N. Y. DEC. EST. LAW § 111(6).

78. *In re* Bernheimer's Est., 106 Misc. 719, 175 N. Y. Supp. 594 (Surr. Ct. 1919); Taylor's Est., 277 Pa. St. 518, 121 Atl. 310 (1923); *In re* Dreier's Est., 204 Wis. 221, 235 N. W. 439 (1931).

79. *In re* Seaman's Est., 333 Pa. 358, 5 A. (2d) 208 (1939).

80. See LORING, *op. cit. supra* note 5, at 127-8.

81. Clark v. Clark, 167 Ga. 1, 144 S. E. 787 (1928); Mobley v. Phinizy, 42 Ga. App. 33, 155 S. E. 73 (1930); *In re* Stump's Est., 153 Misc. 92, 274 N. Y. Supp. 466 (Surr. Ct. 1934); *In re* Grotenrath's Est., 217 Wis. 109, 258 N. W. 453 (1935).

Under such an approach, the trustee is deprived of the power to exercise discretion regarding the advisability of disposing of such securities regardless of the value of the investment or justification for postponing sale.[82] The rule is a natural implication of positive statutory demands in regard to original investments. If deemed exclusive or mandatory for new investments, rules regarding retention will in all likelihood be similar.

2. The trustee is under a duty to convert all non-legals within a reasonable time, unless, in exceptional circumstances, in the exercise of good faith and sound discretion, retention is deemed prudent.[83]

This slight variation of the standard of the trustee's conduct in regard to retention bears close resemblance to that governing original investments under the permissive statute. As in the case of such form of statutory specification, the courts are given greater leeway in protecting the diligent trustee in retaining non-legal securities, and conversely, his liability is thereby rendered more unpredictable.[84]

Both rules as thus expressed by the courts have a "modicum of elasticity"[85] and depression cases well illustrate the varying results obtainable under either. Cataclysmic depreciation in market values and unprecedented general confusion in the security markets imposed severe strains upon former interpretations of "reasonable time,"[86] "exceptional circumstances"[87] and other ambiguous loopholes in the usually stated rules. Both courts and legislatures, in recognition of the dilemma confronting the trustee forced to sell in a chaotic period, and to avoid mass dumping of securities upon an already depressed market, were forced to relax more stringent rules compelling immediate conversion.[88]

82. See Cameron Trust Co. v. Leibrandt, 229 Mo. App. 450, 83 S. W. (2d) 234 (1935); *In re* King's Est., 130 Misc. 296, 224 N. Y. Supp. 283 (Surr. Ct. 1927). *Cf. In re* Balfe's Will, 152 Misc. 739, 274 N. Y. Supp. 284 (Surr. Ct. 1934), *modified*, 245 App. Div. 22, 280 N. Y. Supp. 128 (2d Dep't 1935).

83. *In re* Parson's Est., 143 Misc. 368, 257 N. Y. Supp. 339 (Surr. Ct. 1932); Matter of Clark, 257 N. Y. 132, 177 N. E. 397 (1931). See Notes (1932) 30 MICH. L. REV. 815; (1931) 18 VA. L. REV. 204; (1930) 30 COL. L. REV. 1166; (1930) 5 ST. JOHN'S L. REV. 59.

84. See Bogert, note 73 *supra*.

85. *Ibid.*

86. It was generally stated that one year would be the limit allowed. But *cf.* Cameron Trust Co. v. Leibrandt, 229 Mo. App. 450, 83 S. W. (2d) 234 (1935) (seven months too long); *In re* Seaman's Est., 333 Pa. 358, 5 A. (2d) 208 (1939) (one year too long). But see *In re* Watson's Est., 168 Misc. 135, 5 N. Y. S. (2d) 416 (Surr. Ct. 1938) (10 years reasonable); *In re* Paulsen's Guardian, 229 Wis. 262, 282 N. W. 36 (1938) (15 years justified).

87. That market depreciation alone will not render retention unwarranted see Matter of Winburn, 140 Misc. 18, 249 N. Y. Supp. 758 (Surr. Ct. 1931) ("Wall Street does not set the standard . . .") *In re* Dickinson's Est., 318 Pa. 561, 179 Atl. 443 (1935). But see *In re* Stump's Est., 153 Misc. 92, 274 N. Y. Supp. 466 (Surr. Ct. 1934). (The depression gave no "immunity bath" to the trustee).

88. Large masses of railroad bonds became non-legal with suddenly depreciated dividend records and tonnage miles. To counteract, New York annually passed moratorium

Again, the fact that every settlor is a potential legislator regarding the disposition of his own property supersedes any and all judicially imposed duties on the part of the trustee, or statutory mandates regarding disposal of such non-legal securities. The settlor may direct or permit retention or conversion.[89] The trustee will normally be protected in following permission and liable for failure to follow direction. Inherent in both authority in the instrument and under the many statutes permitting retention, are the basic requirements of prudence and care.[90] Both afford adequate protection for the trustee but are also easily evaded by a court emotionally prejudiced in favor of the cestui. Excused "negligence" may easily become "gross neglect;"[91] "mere errors in judgment" may by a judicious slip of the pen become "inexcusable lack of good faith" or "fraudulent abuse of discretion."[92] As protective guides for the uninitiated trustee, the rules are useless and misleading. As potential arsenals for judicial attack or protection, they serve their purpose. Uniformity in result is necessarily and probably justifiably a lost cause.[93]

III.

Although statutory specification has left much to be desired in determining the risks and extent of the liability of the trustee in the selection of proper investments for trust funds, judicial and legislative requirements of "prudence" do not seem to be susceptible of more exact definition. The advantag-

statutes authorizing retention from 1931 on and finally neatly avoided the whole problem by creating a general authorization to retain all securities. N. Y. DEC. EST. LAW § 111(6).

89. Directions to retain are mandatory. Delaware Trust Co. v. Dupont, 194 Atl. 31 (Del. 1937); Fairleigh v. Fidelity Nat. Bank & Trust Co., 335 Mo. 360, 73 S. W. (2d) 248 (1934). For examples of making consent of beneficiary condition precedent to change, see *In re* Rolston's Est., 162 Misc. 194, 294 N. Y. Supp. 112 (Surr. Ct. 1937); *In re* George's Est., 225 Wis. 251, 270 N. W. 538 (1936); *In re* Olcott's Will, 161 Misc. 890, 293 N. Y. Supp. 267 (Surr. Ct. 1937).

90. Statutory authorization does not excuse imprudent conduct but does supply a meritorious but not conclusive defense. Beardsley v. Bridgeport Protestant Orphan's Asylum, 76 Conn. 560, 57 Atl. 165 (1904) (no surcharge). But see People v. Canton Nat. Bank, 288 Ill. App. 418, 6 N. E. (2d) 220 (1937) (surcharge); Wild v. Brown, 120 N. J. Eq. 31, 183 Atl. 899 (1936) (surcharge). Likewise for authority in the trust instrument. *In re* Allis' Est., 191 Wis. 23, 209 N. W. 945 (1926) ("reluctantly" no surcharge). Authorization to retain settlor's investments cannot justify retaining securities acquired in corporate reorganizations and securities acquired in exchange therefor. "Substantial equivalence" is the usual test imposed. *In re* Richer's Est., 124 N. J. Eq. 228, 1 A. (2d) 213 (1938), *aff'd*, 125 N. J. Eq. 349, 5 A. (2d) 685 (1939); Mertz v. Guaranty Trust, 247 N. Y. 137, 159 N. E. 888 (1928), 13 CORN. L. Q. 638.

91. See Shinn, *Exoneration Clauses In Trust Instruments* (1933) 42 YALE L. J. 359 and cases there collected.

92. Compare opinion of Slater, Surr., in Matter of Clark, 136 Misc. 881, 242 N. Y. Supp. 210 (Surr. Ct. 1930), with the "mere error of judgment" tact used by the Court of Appeals in the same case on appeal. 257 N. Y. 132, 177 N. E. 397 (1931).

93. Dissimilarity in the circumstances of each case make certainty unattainable. SCOTT, *op. cit. supra* note 4, § 230.2.

es of some sort of legislative assistance for the uninitiated trustee and of providing more exacting restrictions than the rule of prudence might seem to require, justifies such legislative action. The uncertainties of the Massachusetts rule rendered his position extremely precarious. Little consolation was to be derived from the fact that upon institutional and empirical standards his investments would be deemed sound if the courts, viewing them in retrospect, did not approve.[94] Drafting the newly defined scope of permissible fields was better accomplished by the legislature, aided by financial experts, than piecemeal by the courts.[95] Undoubtedly, individual instances of the failure of legislative standards to insure selection of sound investments are numerous.[96] To define statutory tests which admit a high percentage of all sound securities without also qualifying a substantial volume of questionable obligations is probably an impossible task. Factors determinative of sound investment policies in varying economic trends are largely incapable of reduction to fixed formulae.[97] Sudden financial depressions play havoc with statutory safeguards, and legislative action is undoubtedly slow and cumbersome in relieving the many problems thus presented to the diligent trustee.[98]

Nevertheless, in spite of this rather impressive array of arguments often asserted against the policy of legislative specification, conservative eligibility tests for prudent trust investments have been instrumental in improving the quality of investment portfolios.[99] For the inexperienced individual trustee, only occasionally presented with the problem, legislative approval has probably constituted a welcome "protective haven" from misleading and elusive judicial standards of prudence and sound discretion.

With the advent of the highly efficient corporate trustee, however, the limitations of the usual legal categories proved unduly restrictive. Lists originally devised for the guidance of the less experienced individual fiduciary tend to impede diligent and prudent efforts to exert assertedly superior abilities.[100] Also, concentration of the enormous mass of trust funds at their disposal within the confined limits of the legal categories tended to raise the prices of such securities and result in artificially low income returns for the beneficiaries with coincidentally decreased fees for the trustee.[101] The constant demands

94. Of course, subsequent events are theoretically not to be used as bases of judgment of a trustee's action in determining the propriety of his investments, but whether admitted or not, such factors are necessarily influential. See Matter of Clark, 257 N. Y. 132, 177 N. E. 397 (1931); Matter of Hurlbut, 210 App. Div. 456, 206 N. Y. Supp. 448 (2d Dep't 1924).

95. Legis. (1936) 49 HARV. L. REV. 821.

96. (1932) 54 TRUST Co. 233. See note 97 *infra*.

97. Edwards, *New Standards For Railroad Securities* (1937) 64 TRUST Co. 174; White and Lawres, *supra* note 8, at 286.

98. See (1931) 51 TRUST Co. 761.

99. See Riddle, *supra* note 1; (1931) 53 TRUST Co. 310.

100. See White and Lawres, *supra* note 8.

101. Riddle, *Trust Investments*, *supra* note 1. Though usually considered a pressing problem, it is highly questionable whether decreased fees or the well-being of beneficiaries

for extension and diversification of the range of eligible investments and increased powers for the corporate fiduciary inspired additional legislation. Several states, in recognition of the peculiar problems and allegedly superior investment abilities of such fiduciaries, enacted extensive statutes solely applicable to trust companies.[102] Many states again extended existing lists for all trustees.[103] Many, cognizant of the inability of legislative action to keep pace with constantly shifting economic trends and to reduce all factors of prudent investment policies to fixed formulae, bestowed special powers in courts and administrative agencies to select and periodically revise lists unrestrained by the usual statutory qualifications.[104] Common trust funds[105] and participation mortgage[106] schemes of multi-ownership in single securities or "pools" of securities created additional investments and offered desirable diversification particularly for the ever-increasing number of small trust estates.[107]

However, in spite of such repeated efforts to appease the demands for extended investment powers, bitter denunciation of the so-called "legislative straight-jackets"[108] continue to come from corporate trustees in the name of "undue restriction" and "inflexibility" of legislative standards. Restrictive lists are said to inhibit the proper exercise of discretionary powers.[109] The policy of usually demanding investments in fixed-obligation bonds and mort-

so often expressed, inspires the rationalization. See Carpenter, *The Fixed-Income, Annuity, And Modernized Types of Trusts* (1938) 5 LAW & CONTEMP. PROB. 368.

102. *E.g.*, ORE. CODE ANN. (Supp. 1935) § 22-1214; N. Y. BANK. LAW § 100c.

103. *E.g.*, PENN. STAT. ANN. (Purdon's, 1930) tit. 20, §§ 801–817; N. J. REV. STAT. (1937) § 3:16-6--3:16-18.

104. New York and Connecticut long made it the duty of the banking commissioner to issue periodically lists of conforming securities. N. Y. BANK. LAW § 35; CONN. GEN. STAT. (1930) §§ 3996-4003. See (1931) 51 TRUST CO. 659; (1931) 52 TRUST CO. 696. But trustees were not relieved of the duty of making their own investigations of their investments. (1935) 59 TRUST CO. 657. Power to originally authorize and select "legals" however, is a new phenomenon and little is known of the success or failure of such plans. See White and Lawres, *supra* note 8, for full consideration of the advantages and disadvantages of administrative selection. Unequipped for the duties, many administrative agencies have been reluctant to exert such powers. Communications to YALE LAW JOURNAL from various state banking departments.

105. See for full discussion, Bogue, *Common Trust Fund Legislation* (1938) 5 LAW & CONTEMP. PROB. 430; Ward, *Problems In The Administration of Common Trust Funds, id.* at 453; (1933) 11 HARV. BUS. REV. 253; Barclay, *Commingled Funds Offer Broader Scope For Trust Service* (1931) 53 TRUST CO. 615.

106. See McKinney, *The Legality of Participating Mortgage Certificates For Trustees* (1915) 24 YALE L. J. 286; Simpson, *Participation Certificates Permitting Substitution of Securities As Legal Investments For Trust Funds* (1930) 7 N. Y. U. L. Q. REV. 950; Comment (1932) 41 YALE L. J. 455.

107. For excellent factual and legal study of participating mortgage plans, see Comment (1936) 45 YALE L. J. 857.

108. Andrews, *Flexibility or Legislative Straight Jackets In Investment of Trust Funds* (1929) 48 TRUST CO. 413; (1931) 51 TRUST CO. 761; (1932) 54 TRUST CO. 233, 329, 473.

109. *Ibid.*

gages is often declared to run counter to well-accepted investment theory. The purchase of common stocks as a "hedge" against the dangers of inflationary periods is said to be a sound investment policy, yet prohibited by the usual, legal lists.[110] Unsecured investments in the trust portfolio are supposed to offer desirable diversification but seldom are included in the permissive categories.[111]

Further extension of the legal lists, however, in accordance with the demands of the supposed investment experts, would seem to be both undesirable and unnecessary. Constant extension of the permitted fields must include more dangerous and speculative securities and subject the beneficiaries to increased dangers of disastrous losses.[112] Less competent trustees may be tempted to indulge in speculative enterprises which require more constant supervision and intensive examination than they are equipped to control. The policy of protecting the beneficiaries and at the same time offering well-defined "protective havens" for the inexperienced trustee in his quest for prudent trust investments would seem to justify sacrificing the attractive but often questionable investment theories propounded by the larger trust companies. Further, the usual key-stones of trust company attack—undue restriction and inflexibility—would not seem to be borne out by actualities. In accordance with the asserted desires for unrestrained discretion in handling trust accounts, corporate fiduciaries have for years urged that complete discretionary powers and exculpatory clauses be incorporated in trust instruments.[113] Typical investment clauses attempt completely to obliterate any and all judicial or statutory limitations upon their powers in disposing of the funds in their control. Judicial restrictions and standards evolved for the protection of beneficiaries over a period of four centuries are simply and completely wiped away by such authorization induced from the settlor by trust company officials and lawyer-draftsmen.[114] "Restriction" and "inflexibility" would thus seem to be largely an unwarranted obsession. Rather, the obvious inspiration for such continued assaults upon the legislative safe-guards would seem to be a desire to obtain the protective stamp of legislative approval for more productive but also more dangerous investment schemes and policies.

Since legislative specification performs no necessary function for fiduciaries thus actually unrestrained in their handling of trust funds, complete

110. See generally Riddle, *supra* note 1; (1930) 50 TRUST CO. 427; Woodruff, *Legal And Investment Standards of Trustees* (1935) 4 FORD. L. REV. 391. But see Headley, *A Trustee In A World of Changing Values* (1938) 5 LAW & CONTEMP. PROB. 355; (1930) 51 TRUST CO. 185; (1931) 53 TRUST CO. 319.

111. *Ibid.*

112. (1931) 51 TRUST CO. 489.

113. Stephenson, *Trust Investment Provisions Which Have Worked Well* (1938) 5 LAW & CONTEMP. PROB. 377; Stephenson, *Investment Provisions Of Wills and Trust Agreements* (1938) GRAD. SCHOOL OF BANKING. See Leach, *Lessons From the Depression In the Drafting of Wills And Trusts* (1933) 18 MINN. L. REV. 27.

114. See generally Leach, *supra* note 113. But see (1926) 26 COL. L. REV. 453.