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Some Aspects of the Obligations of New York Fiduciaries with Respect to the Making of Investments, I

Louis C. Haggerty

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SOME ASPECTS OF THE OBLIGATIONS OF NEW YORK FIDUCIARIES WITH RESPECT TO THE MAKING AND RETENTION OF INVESTMENTS, I

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The Obligation and Authority to Invest

As a general rule it is the duty of a fiduciary to see to it that the funds in his hands are kept in productive use.¹ He may be held liable if he fails to do so through neglect,² but not if the failure is in spite of reasonable diligence.³ Each case must depend upon and be governed by the peculiar facts and the surrounding circumstances.⁴ If the instrument creating the estate should fail to give express authority or direction to invest the principal, the direction to do so may be implied from all its terms and provisions as for instance, where there is a direction as to the application of the income⁵ and a direction to invest in-

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Unless otherwise noted, the Miscellaneous and New York Supplement citations are of opinions of the Surrogates' Courts of the State of New York.

1. The doctrine has been long established. It is difficult to improve on the way in which it has been stated in the earlier decisions. Thus, in DePeyster v. Clarkson, 2 Wend. 77, 87 (N. Y. 1828) the Chancellor said: "It is the duty of trustees and guardians to keep the moneys belonging to the trust estate properly invested. Circumstances may justify a deviation from that duty, and those circumstances may be so strong as to require the trustee, in the exercise of sound discretion, to refrain from making investments but those circumstances rarely occur; and when they do, the trustee is bound to state them to the court as the reasons for his otherwise culpable neglect." In Dunscomb v. Dunscomb, 1 Johns. Ch. 501, 510 (N. Y. 1815), the Chancellor said that: "... the rule is well settled that executors and all other trustees are chargeable with interest if they have made use of the money themselves, or have been negligent, either in not paying the money over, or in not investing it, or loaning it so as to render it productive. ... The rule is founded in justice and good policy; it prevents abuse and it indemnifies against negligence."


come may be implied from a direction that income be accumulated. If, however, the will expressly or by judicial determination forbids the making of investments, the fiduciary may not invest even in those permitted by statute, and if he does so, albeit in the best of faith, he will be responsible for any loss that may result. If the phraseology with respect to investment powers is unusual, a careful study of the situation is recommended.2

But while every fiduciary, unless prohibited by statute or express provision, has the power to invest and re-invest, the extent of his obligation to do so will vary with the purposes of his office. A fiduciary whose function it is to receive and retain, such as a trustee, has the paramount duty of investing the trust estate and of keeping it reinvested. One whose function it is to collect and distribute, such as an executor or administratrix, has the paramount duty of reducing the estate to cash within prescribed periods in order to pay debts, estate taxes, legacies and administration expenses as they become payable. Hence, while courts have stated that an executor3 and an administratrix4


7. In Matter of Trimbey, 151 Misc. 37, 271 N. Y. Supp. 703 (Onondaga Co. 1934) the testator had directed that certain moneys be deposited with a corporate fiduciary as trustee; and authorized and directed it "... as such Trustee, to pay over the income from the amount so deposited to my daughter ..." The trust company invested the money in a mortgage which was a legal investment. But the court held that the trustee had no authority to make investments of any kind, that the testator intended that the moneys should be kept on deposit and that the beneficiary should receive whatever interest the trust company, as a trust company, paid on its deposits generally, and that the trustee should be surcharged for the loss which had occurred.

8. In Villard v. Villard, 219 N. Y. 482, 498, 114 N. E. 789, 793 (1916) the court said: "... it may also be desirable or even the duty of an executor to invest uninvested funds in his possession as executor. ... It is not, therefore, entirely correct to say that an executor as such has no authority to make investments." This serves to over-rule the holding in Matter of McDowell, 97 Misc. 306, 325, 163 N. Y. Supp. 164, 174 (Chemung Co. 1916) that "The general rule is that executors as such have no authority to invest the funds of an estate."

9. In Stark v. National City Bank, 278 N. Y. 388, 393, 16 N. E. (2d) 376, 378 (1938) the court said: "An administratrix is under a duty to distribute the assets of an estate or their proceeds after payment of taxes, administration expenses and debts. ... Pending such administration, she might, we assume, invest money in the estate in the 'kind of securities' in which fiduciaries are authorized to invest trust funds." It is difficult to conceive of less emphatic language.
and an administrator c.t.a have the powers to make investments, they have done so in carefully guarded language, and have limited the advisability of investing to special situations.

At one time the conflict between an executor’s special duty to liquidate the estate for distribution and his general duty to keep his cash at work could be solved by the simple means of depositing the accumulated cash in an interest-bearing bank account. One executor who kept about $3,500.00 in a non-interest bearing account for 14 years was charged with interest at the rate then being paid by Liberty Bonds of happy memory. As a matter of fact, there were numerous instances in the past where the failure of an executor or administrator to keep his cash at work caused a surcharge. The rate of interest which the surcharged fiduciary had to pay varied with the facts, as did the basic question of any liability at all. But the doctrine was applied reasonably. Thus, cash could be kept in a non-interest bearing checking account if needed for current expenses or if awaiting distribution.

10. In Matter of Buck, 184 Misc. 29, 52 N. Y. S. (2d) 294 (Westchester Co. 1944) it was stated that the making of investments by an administrator c.t.a. “... was not necessarily improper.” A temporary administrator has no power in himself to make any investments. Baskin v. Baskin, 4 Lans. 60 (Gen. Term, 4th Dep’t 1871). But he can make them by an order of the Surrogate.


14. If the cash was not used to the personal advantage of the fiduciary, he was charged only with the average rate of interest paid by savings banks. Matter of Bradley, 2 N. Y. Supp. 751 (New York Co. 1888); Livermore v. Wortman, 25 Hun. 341, 344 (1st Dep’t 1881). But if the fiduciary mingled the funds with his own, interest might be fixed at the legal rate. Matter of Mayer, 132 Misc. 384, 385, 229 N. Y. Supp. 638, 639. (Rockland Co. 1928); Matter of Thorp, 31 Misc. 361, 362, 65 N. Y. Supp. 575, 576 (Ontario Co. 1900). Cases in which the fiduciary deposited the estate funds in a bank in which he had a personal interest whether as officer, director or stockholder, presented special problems. If the bank paid interest to other depositors but not to the estate, the fiduciary was liable to a surcharge. Matter of McKay, 5 Misc. 123, 134, 25 N. Y. Supp. 725, 732 (Cattaraugus Co. 1893); Matter of Babcock, 9 N. Y. Supp. 554, 555 (Cattaraugus Co. 1899). But if none of the depositors received any interest on their deposits, the fiduciary was excused from liability to the estate. Matter of Sexton, 61 Misc. 509, 571, 115 N. Y. Supp. 973, 975 (Wayne Co. 1903); Matter of Johnson, 57 App. Div. 494, 501, 503, 67 N. Y. Supp. 1004, 1009 (4th Dep’t 1901).

Today, a different situation exists. The courts have placed increased emphasis on the obligation of an executor to liquidate sufficient of the estate to pay debts, legacies and estate taxes as they become due.17 In addition, the obligation imposed on the executor or administrator to earn money has been de-emphasized in a practical way by changed economic conditions. The ordinary checking account does not yield any interest and obviously unless the administration of the estate is to be long drawn out, the investments, if any, which an executor or administrator makes should be in bonds which will mature without fail simultaneously with the obligations of the estate,18 which means short-term bonds of the highest grade on which the return is slight.

The law provides, or perhaps imposes, a solution for this problem upon the trust company who acts as executor or administrator. It must allow the estate interest on uninvested funds at a rate fixed by statute.19 The individual executor or administrator must make up his own mind what to do. He may have built up a substantial amount of cash for the payment of debts, taxes and similar charges or through the sale of assets whose retention was deemed inadvisable. The problem of administering the cash fund so created presents and exacts the same test as do other administrative problems: the test of prudence and diligence.20 If a faithful and diligent executor or administrator, after careful consideration of all the factors involved, finds reasonable grounds for rejecting any media of investment of the cash in his hands, it is reasonable to assume that the court will support the judgment so arrived at.

The Investments Which May Be Made

A fiduciary may invest the estate committed to his care only in such securities as are authorized by the creator of the estate, or, in the absence of any such authorization, in such securities as are authorized for fiduciary investments by the statutes of the State.21 The rule is

17. As for example Matter of Witkind, 167 Misc. 885, 4 N. Y. S. (2d) 933 (New York Co. 1938) Delehanty, S.
18. A suggestion along these lines will be found in Matter of Schroder, 176 Misc. 1024, 1029, 29 N. Y. S. (2d) 754, 759 (Kings Co. 1941) Wingate, S.
19. N. Y. BANKING LAW § 100-b (4). The statute distinguishes between fiduciaries in general and an executor or administrator. Interest at the rate prescribed therein begins sixty days from its receipt, except that in the case of "... a trust company acting as executor or administrator, interest shall not be allowed and the grace period of sixty days herein provided shall not be deemed to begin until five months after the date of issuance of letters."
part of the public policy of the State. The pertinent statutes are: for executors, administrators and trustees, Section 111 of the Decedent Estate Law and Section 21 of the Personal Property Law; for guardians, Section 88 of the Domestic Relation Law and Section 111 of the Decedent Estate Law; for Committees of Incompetents, Section 1384-L of the Civil Practice Act.

The right of a person to determine how his estate may be invested by his fiduciary was recognized both before the enactment of the legislation which created "legals" and afterwards when it was contended that a clause permitting investments in "non-legals" was void as against public policy. The courts have been explicit in this respect. The Appellate Division of the First Department has said:

"It is fundamental Law that a testator or the creator of a trust has unlimited authority to direct how his money may be invested by his trustees or may leave the manner of such investment completely in the discretion of such trustees."

This is in keeping with the statement attributed to a vice-chancellor some time ago that "... every testator by the law of the land is at liberty to adopt his own nonsense in disposing of his property."
On the other hand a testator may narrow the field of investments even further than has the legislature and may bar his fiduciary from making investments which the statutes themselves permit.\textsuperscript{27} If his fiduciary nevertheless invests in a legal investment barred by the testator, he will incur a responsibility and potential liability no less great than if he had invested, without authority, in non-legal securities.\textsuperscript{28} This is because "In making investments of trust funds the trustee is under a duty to the beneficiary to conform to the terms of the trust."\textsuperscript{29} It is suggested, however, that a prohibition against the purchase of government bonds might be void as against public policy.\textsuperscript{30}

The violation of an administrative provision, such as the failure to obtain the two appraisals required by a will, will make an investment an unauthorized one with the resultant liability accruing to the fiduciary.\textsuperscript{31}

A fiduciary who, without authority, makes an investment outside of the class permitted to him becomes a guarantor of it and absolutely liable for any loss that may be sustained; and this, in spite of all the care and prudence which he may have exercised in its selection. "He

\textsuperscript{27} Matter of Goebel, 177 Misc. 553, 554, 31 N. Y. S. (2d) 7, 9 (New York Co. 1941) Foley, S.

\textsuperscript{28} In Matter of Jeremiah, 180 Misc. 692, 693, 42 N. Y. S. (2d) 330, 331 (New York Co. 1943) Delehanty, S., a trustee who was permitted to invest in mortgages on property "...in the City of New York or in the City of Brooklyn..." by the terms of will made in 1883, was surcharged for a mortgage on Queens County real estate, because Queens County was not a part of either the City of New York or the City of Brooklyn at the time when the will was made and the testator died. In Matter of London, 104 Misc. 372, 376, 171 N. Y. Supp. 981, 983, aff'd, 187 App. Div. 952, 175 N. Y. Supp. 910 (1st Dep't 1919), a fiduciary limited to railroad bonds was surcharged for buying New York City bonds, legal by statute. He was, however, exonerated from liability for investing in Liberty Bonds. It was a war-time purchase and Surrogate Cohalan said that the testator would not have intended to bar his trustee from aiding his country in time of need. In Matter of Irwin, 59 Misc. 143, 144, 112 N. Y. Supp. 205, 206 (New York Co. 1908) Thomas, S., a trustee limited to real estate mortgages and railroad bonds was surcharged for investing in New York City Bonds, which were legal by statute. Other cases and of like effect are, Matter of Loomis, — Misc. —, 45 N. Y. S. (2d) 146, 150 (Westchester Co. 1943) Millard, S.; Matter of Goebel, 177 Misc. 553, 31 N Y. S. (2d) 7 (New York Co. 1941) Foley, S.; Matter of Olney, 255 App. Div. 195, 197, 7 N. Y. S. (2d) 89, 93 (4th Dep't 1938); Matter of Trimbey, 151 Misc. 37, 271 N. Y. Supp. 703 (Oneida Co. 1934).

\textsuperscript{29} Matter of Goebel, 177 Misc. 553, 554, 31 N. Y. S. (2d) 7, 9 (New York Co. 1941) Foley, S.


\textsuperscript{31} Matter of Diamond, 163 Misc. 611, 614, 297 N. Y. Supp. 969, 973 (New York Co. 1937) Foley, S.
acts at his peril when he disregards statutory limitations upon his power." Good faith will not relieve a fiduciary from the liability accruing from an unauthorized investment, nor will honesty exonerate him, nor the excellence of the purpose for which the investment was intended. The very fact that an investment is unauthorized means that the fiduciary must bear the loss. And this without any right to any profit which might arise from it.

It is not necessary to show that an unauthorized investment has resulted in a loss to the estate in order to impose a liability upon the fiduciary. He may be surcharged for its cost without waiting to see if a loss will result. It should, however, be remembered that when a fiduciary is surcharged for the cost of an investment remaining in his hands, he is entitled to receive back the investment for his own account upon paying the amount of the surcharge.

**Determining the Investment Powers**

Obviously, one of the first things that a fiduciary should do is determine the extent of his investment powers. This is not always easy. It is not merely a matter of examining the language of the will itself. Even though the provisions are, on their face, clear and unequivocal, they may have been rendered inoperative by factors outside the will. For instance, if a testator fails to make provision for an after-born child, with respect to which he dies intestate, the investment powers in the will do not apply to the share of the after-born child. Another instance in which the language of the will may be affected by circumstances outside of the will is where a successor or substituted fiduciary takes the place of the one named in the will. In the absence of explicit language with respect to the matter, the question of whether or not a successor or substituted fiduciary may exercise the powers given to the original fiduciary is a question of construction and of the testator's intention. There is no "rule of thumb." Each case must be determined

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34. Matter of Mattison, 17 N. Y. S. (2d) 735, 739 (Westchester Co. 1949).
40. Smith v. Floyd, 193 N. Y. 683, 87 N. E. 1127 (1908). For an exhaustive review of
in the light of the peculiar facts and circumstances surrounding it. It should be remembered, however, that the general doctrine that a power which involves a personal element of confidence does not pass to a successor is not always applied with respect to a successor fiduciary. The courts have adopted a liberal attitude in finding evidence of an intent by a testator to clothe a substituted fiduciary with powers which might appear at first impression to be founded on personal considerations and based upon the confidence which the testator had in the particular individuals named in the will. Thus, the fact that a trust would probably continue beyond the life of the trustee named by the testator has been given weight by the courts in arriving at the determination that the testator intended that the successor fiduciary should have all the powers granted to the trustee originally named. But in the majority of cases, the difficulty in determining the investment powers of the fiduciary arises from the use of vague, ambiguous, and inexact language by testators, some of whom seemingly try to make it difficult for everyone else to determine what they mean.

As with all matters of construction, the determination of the extent of the investment powers which a testator intended to give to his fiduciary involves the examination and study of the entire document. The language used by the testator is of varying degrees of importance. Sometimes it is conclusive; in other instances it is subordinate to attendant circumstances. Elements such as the relationship between the testator and the beneficiaries or between the testator and the fiduciary, or the character of the testator's own investments may be of greater value.
in determining the testamentary intent than the precise words which were employed in concealing it.

It should be realized that very often, the words used or the phrases employed should not be analyzed literally, because they are legal "cliches" if not idioms, and hence meaningless if considered by themselves. Thus any number of testators will tell their fiduciaries to invest in their "best judgment" or "for the best interests" of the estate. But not only is a fiduciary obligated by law to use his "best judgment" and work for the "best interests" of his estate but it is inconceivable that any testator would wish his executor or trustee to furnish anything less than his best judgment or operate for anything less than the best interests of his estate.

Courts have differed widely on the interpretation to be placed on vague words and phrases. Moreover, since collateral circumstances are also to be considered, it is impossible to tell in some instances to what extent the words, and to what extent the circumstances, were the controlling factors. A few cases in which the courts have been called upon to determine the investment powers of fiduciaries are submitted herewith but with the warning that they constitute precedents for avoiding the use of the words and phrases construed, rather than precedents for the construction actually adopted by the courts. The word "legals" following the words construed indicate that the courts held that the fiduciary was limited to statutory investments, or, if the decision antedated the statute, to investments permitted to fiduciaries by the then prevailing doctrine. Naturally, the word "non-legals" indicates that a contrary result was reached.

"Invested in such securities as to the said executors shall seem best"; non-legals, but other factors were considered; 45

"invest and re-invest as they shall deem wise and judicious"; non-legals, but the court considered the testator's own investments; 46

"in such ways and securities as to them shall seem wise and discreet"; non-legals, the language seemingly being controlling; 47

"invest and re-invest the same as to it shall seem best"; non-legals, the court saying that the language gave the fiduciary "an extremely broad authority"; 48

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45. Ibid.
“in any security real or personal which they may deem for the benefit of my estate”; non-legals; 49
“in such suitable manner as may be for the best interests of my estate to be determined by my said executor”; legals. The language was controlling. The referee had held that the fiduciary was not confined to legals, stressing the word “determined”. The Surrogate thought that “suitable” was controlling and held to the contrary; 50
“in first mortgage notes, or other first-class securities which will bear as high a rate of interest as said trustees shall deem consistent with the safety of the investment”; legals; 51
“to bring in the largest income compatible with reasonable safety”; non-legals; 52
“in any other such securities as to it or to them shall seem safe and proper”; non-legals; 53
“in other lands or buildings, or bonds and mortgages or in such other securities as they shall deem safe and for the greatest benefit of my daughters”; legals; 54
“at interest in such manner and upon such security and at such rate of interest as to him, in his discretion, shall seem proper and suitable”; legals. The court said that the language conveyed a general discretion and no more and did not authorize the trustee to make any specific investment or to transcend the general rule applicable to trustees. 55 This followed the reasoning of King v. Talbot 56 where the testator had entrusted the administration of his estate to the “discretion” of his fiduciaries. The court held that the language:

“... neither added nor in any wise affected the duty and responsibility of these executors; without it, they were clothed with discretion; with it their discretion was to be exercised with all the care and prudence belonging to their trust relation to the beneficiaries”.

“in the exercise of their sound judgment and “discretion” in “well selected, and well secured, as distinguished from speculative securities or investments”; legals. The court stressed the importance of “well-secured” and minimized the use of the word “discretion” because it was reviewable. 57 This

50. Matter of Cant, 5 Dem. 269, 271 (New York Co. 1886) Rollins, S.
52. Matter of Leonard, 118 Misc. 598, 600, 193 N. Y. Supp. 916, 918 (Westchester Co. 1922) Slater, S.
53. Matter of Kane, — Misc. —, 25 N. Y. S. (2d) 988. (Nassau Co. 1941) Howell, S.
56. King v. Talbot, 40 N. Y. 76, 78 (1869).
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is rather close reasoning. It might be pointed out that if the testator intended that his fiduciaries should be limited to statutory investments, he could have accomplished that end by the very simple device of saying nothing at all about their investment powers or policy. If the reasoning of the court is correct, it follows that the testator used a number of words to say nothing.

"In accordance with their best judgment and discretion"; non-legals;\(^59\)

to buy, sell and exchange such securities as in his discretion, or that of his successor or successors in the trusts herein, may seem for the best interests of my estate"; non-legals.\(^59\)

The use of the word "discretion" is given more weight currently than in the earlier cases. The failure to use it has been advanced in some instances as a reason for deciding that the testator intended that the fiduciary be limited to legals.\(^59\)

Sometimes the testator will endeavor to express his intentions as to the investment powers which his fiduciary may exercise by applying adjectives to the type of securities which may be acquired. As for example:

"in good, sound, dividend paying securities"; non-legals, but the court was influenced by the fact that the testator did not own any legals;\(^61\)

"in their discretion in good interest bearing securities"; non-legals. The court said that the testator was trying to say: "securities bearing good income", thereby intending good non-legals.\(^62\)

Then, there are the general clauses, such as granting "full power to do any and all things that may be requisite and proper in the settlement of my estate, including the keeping of my estate safely invested." Such a clause was construed as granting no additional investment powers over the statutory powers.\(^63\) Another testator gave to her trustee the power to invest "as he may be advised." This is a phrase which may be interpreted either literally or colloquially. The court adopted its literal meaning to the extent of holding that the testatrix wished her

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trustee to consult about prospective investments and obtain such advice as he might find available before making them but to be free nevertheless from statutory limitations.64

Among the collateral circumstances considered is the relationship of the testator to the beneficiaries of the estate. When a court was called upon to interpret the investment powers of a trustee who was authorized to invest in securities which yielded "the most income obtainable with safety" (and it might be added that untold fortunes await any fiduciary who can select such securities) and it appeared that the beneficiaries of the trust were the testator's wife and children, the court took into consideration his evident concern about the income which his family would have to live on in ruling that the trustee was not confined to legals.65

Another factor which the courts consider is the character of the investments which the testator himself made during his lifetime.66 This is a reasonable theory, and the fiduciary should adopt it in administering the estate. If, for example, a testator leaves an estate containing non-legal bonds and preferred stocks but no common stocks and the court gives weight to the testator's own investments in deciding that general powers of investment had been given to the fiduciary, the trustee, in turn, would do well to limit the estate investments to the same character of bonds and preferred stocks and refrain from investing in common stocks, in spite of a legal right to do so. One court has wisely suggested this practice67 and it can be followed to advantage.

The relationship between the testator and the fiduciary and factors such as the character and business experience of the fiduciary are also

64. Matter of Backus, 175 Misc. 13, 22 N. Y. S. (2d) 613, 622 (Ontario Co. 1940) Cribb, S.
matters for consideration. The investment experience of the fiduciary, in one instance, and the fact that in another case, the fiduciary named had managed the testator's investments in the latter's lifetime were taken into consideration by the court in determining the extent of the powers which were given.  

When testators describe the kind of investments which their fiduciaries are to be authorized to make, they are apt to cause trouble and confusion unless they are precise and definite in their language. The very word "securities" is broad and elastic and had to be construed. When used without qualifying language, it is not limited to bonds but includes stocks, whether common or preferred. But "safe and stable interest bearing securities" do not include stocks because stocks do not bear interest.  

It is not surprising to find that the elastic phrase "of like character" should require construction and the court held that an authorization to invest in "government bonds or securities of like character" meant United States, State and high grade municipal bonds but not guaranteed mortgages or railroad bonds, even though they were "legals."  

**The Rule of Strict Construction**

After considering some of these decisions, it will come as no surprise to be told that the courts have adopted a rule of strict construction in determining the extent of investment powers. A fiduciary must

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70. Matter of Morris, 153 Misc. 905, 907, 276 N. Y. Supp. 254, 258 (Montgomery Co. 1934). The court gave weight to the omission of any reference to "... income or dividend paying securities."  
be able to establish convincing proof in order to persuade the court that he is not limited to "legals" and it has become a well recognized doctrine that "... a departure from the normal course of the trust is only to be had upon clear and controlling direction in the will"; that the fiduciary "... must be able to point to a clear testamentary authorization, broad enough to cover the particular act of investment or retention performed," and that "only express and unequivocal language" suffices to dispense trustees from the obligations of the statute. But there is a slight suggestion in an earlier case that the court will be more strict in construing investment powers as an abstract matter in a construction proceeding, than it will be in a contested accounting, if the administration of the fiduciary who exercised them has been marked with fidelity and diligence.

The rule of strict construction is applied also to specific conditions imposed upon the purchase of investments. Thus, when a fiduciary is authorized to invest in securities of corporations which have paid dividends on their common stock at a specified rate for a specific period, the dividends must be cash dividends and the securities to be purchased must have been in existence during the period over which the dividends shall have been paid. And when a fiduciary is authorized to invest in bonds of a corporation which has not defaulted in interest for a specified period, he will be limited to a specific issue of bonds which have been issued and outstanding over the period in question and on which interest has been paid as prescribed, the non-default of the company in paying interest on other obligations being insufficient to meet the test. Territorial limitations on mortgage investments will also be enforced strictly. Thus, in a case already referred to, when a testator, who made a will in 1883 and died in 1888, authorized his trustee to invest in mortgages on property in the City of New York or in the City of Brooklyn, the trustee was surcharged for investing in 1937 and

77. Matter of Siegbert, N. Y. L. J., Sept. 25, 1942, p. 740, col. 6 (New York Co.) Foley, S.
in 1938 in a mortgage in the Borough of Queens. Although Queens was a part of New York City when the investment was made, it was not within either New York or Brooklyn when the will was made.86

Occasionally, however, the rules of strict construction will be relaxed. Thus, in one instance, trustees, who were permitted to invest in Government, State and Municipal bonds and who reported to the court in 1939 that they found it difficult to find suitable investments within this field, were authorized to invest in Federal Farm Loan, County and Port of New York Authority bonds and those bonds guaranteed by the United States government which were legal for trustees.87 The same will authorized the trustees to invest in bonds and preferred stocks of industrial companies which had an uninterrupted interest or dividend record for ten years before their purchase. The trustees reported to the court that they found it difficult to find desirable bonds and preferred stocks which met this particular requirement, because a number of companies in which the trustees desired to invest had been able, within the ten year period preceding 1939, to refund and re-finance their bonds at lower interest rates, or perhaps had merged or consolidated with other concerns, without interrupting dividend payments. These facts attested to their financial strength, and the court authorized the trustees to invest in bonds issued in exchange for, or in refund of bonds, formerly outstanding, even if the bonds so purchased had been outstanding less than ten years "... but where interest has been regularly paid for more than ten years if there be taken into account the period during which the predecessor bonds were outstanding ...",88 and also to invest in preferred stock of corporations which had been in existence less than ten years which resulted from a merger, consolidation or acquisition of assets of a predecessor corporation "... and where dividends have been paid regularly for more than ten years, if there be taken into account the dividend record of such predecessor corporation. ..."89

There is at least one question of interpretation of investment powers in which the rule of strict construction has not been adopted. It seems

78. Matter of Jeremiah, 180 Misc. 692, 42 N. Y. S. (2d) 330 (New York Co. 1943) Delehanty, S. The date of the will is of course a factor for consideration. Thus a reference to "securities that shall be tax exempt under the laws of the State of New York," contained in a will made prior to the enactment of any income tax laws, was construed as meaning securities exempt from the personal property tax, since a personal property tax law was in effect when the will was made. Matter of Phelps, 184 Misc. 278, 55 N. Y. S. (2d) 815 (New York Co. 1944) Foley, S., aff'd, 269 App. Div. 768, 55 N. Y. S. (2d) 363 (1st Dep't 1945).


81. Ibid.
to be well established that if a fiduciary has testamentary power to invest the principal of his trust estate in non-legal securities, then, in the absence of any language displaying a contrary intention, he may also invest in non-legals the income in process of accumulation.82

The doctrine that investment powers should be strictly construed is so firmly entrenched that possibly it is no longer open to attack. Yet, it is a judge-made doctrine and its wisdom is not without question. If a testator is completely silent upon the matter of investment powers, it follows that his fiduciary is limited to statutory investments. If he says anything at all, except to emphasize a limitation to legals or to reduce the field of investment even more narrowly, it seems reasonable to assume that at least possibly, if not probably, he is expressing a wish and desire that his fiduciaries should not be limited by the statute. Otherwise what he says is quite unnecessary. It is true that testators should not be encouraged to indulge in vague and general language in prescribing the investment powers which their fiduciaries may exercise, particularly because it is easy to state unequivocally whether or not the fiduciary is to be limited to the investments authorized by the statutes. But if a testator has spoken and has left his meaning in doubt, it might be material to ask: "Since, by silence, the testator could have limited his fiduciaries to legals, why did he say anything at all?"

Standards of Care—The Rule of King v. Talbot

The degree of care which a fiduciary must employ in making and retaining estate investments may be set forth in a few words. He is bound to employ such diligence and prudence as in general prudent men of discretion and intelligence in such matters employ in their own like affairs.

The rule is taken from the opinion of the Court of Appeals in King v. Talbot, decided in 1869,83 and although purely judge-made, it has been given the force and effect of a statute84 and has made King v.}

83. 40 N. Y. 76 (1869).
84. In Matter of Wotton, 59 App. Div. 584, 69 N. Y. Supp. 753 (1st Dep't 1901), aff'd, 167 N. Y. 629, 60 N. E. 1123 (1901) the court said: "It has been settled in this state a trustee holding a fund for investment is bound to put it in government or real estate securities, King v. Talbot, supra. The rule laid down in that case has been enforced by the courts and trustees have been held to that form of investment except so far as the legislature has from time to time authorized another investment by trustees in certain other specified securities." In Matter of Jarvis, 110 Misc. 5, 13, 180 N. Y. Supp. 324, 329 (Westchester
Talbot the leading case with respect to the obligations of a fiduciary. The facts presented to the court were simple. A testator had created three trusts for the benefit of his children. At the time, there was no statute establishing the class or kind of securities in which a fiduciary might invest. The trustees invested part of the funds in common stocks which, in the language of the court, "were in good repute, and were considered by men, upon whose judgment it was proper to rely, as safe and desirable investments." The trustees bought them in good faith. They had invested and kept invested their individual funds in similar investments. When the trustees accounted, the remaindermen objected to the common stock investments and asked that the trustees be required to take them back at their original cost. The primary issue before the court for determination, therefore, was whether the trustees, without authority from the testator, were justified in investing estate funds in stocks of private corporations. The court held that fiduciaries could not invest in stocks without express authority. The determination so made has continued in force and effect both by statute and by judicial interpretation.

The reasons advanced do not reflect modern opinion and conditions. Judge Woodruff's objections to stocks as investments for fiduciaries were two-fold; it involved a surrender by fiduciaries of control over their funds and stocks were not maturing obligations. Thus, he said:

"The moment the fund is invested in bank, or insurance, or railroad stock, it has left the control of the trustees; its safety and the hazard, or risk of loss, is no longer dependent upon their skill, care or discretion, in its custody or management, and the terms of the investment do not contemplate that it will ever be returned to the trustees."

It does not detract from the importance of King v. Talbot to recognize that these objections are today obsolete and that some of the factors.

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Co. 1920) Slater, S., the court said that certain securities did not fall within the class of legal investments as determined by the legislature of this state, and the law laid down in King v. Talbot and Matter of Wotton, N. Y. DEC. ESTATE LAW § 111; N. Y. PERS. PROP. LAW § 21.

85. Its doctrine "... is recognized as the universally guiding principal respecting the conduct of testamentary and intestate fiduciaries." Matter of Kruger, 139 Misc. 907, 249 N. Y. Supp. 772 (Kings Co. 1941).

86. The first such statute was contained in c. 65 of the Laws of 1889.

87. N. Y. DEC. ESTATE LAW § 111; N. Y. PERS. PROP. LAW § 21.

88. In Mertz v. Guaranty Trust Co., 247 N. Y. 137, 159 N. E. 888 (1938) Judge Cardozo wrote at p. 144: "A trustee is without authority to invest in the shares of a business corporation or even to continue such an investment made by another, unless authority so to do is conferred by the creator of the trust. King v. Talbot."

89. King v. Talbot, 40 N. Y. 76, 83 (1859).
which Judge Woodruff considered unfavorable are now looked upon as desirable. So far as the recall of the investment is concerned, listed stocks are today at least as liquid as bonds and unlisted stocks, are more liquid than real estate mortgages. And as for the surrender of control over the estate funds, there is the counter consideration that a trustee who invests in the stock of a well run corporation will get the services and experience of skillful and experienced managers. But the importance of King v. Talbot lies primarily in the standards which it promulgated for fiduciaries in administering the affairs of their estates. Judge Woodruff said:

"Whether it has been declared by the courts or not, whether it has been enacted in statutes or not, whether it is in familiar recognition in the affairs of life, there appertains to the relation of trustee and cestui que trust, a duty to be faithful, to be diligent, to be prudent in an administration entrusted to the former in confidence in his fidelity, diligence and prudence."91

Judge Woodruff then proceeded to say, and what he wrote has been repeated by other courts time and time again, that in the administration of a trust estate:

"... the just and true rule is, that the trustee is bound to employ such diligence and such prudence, in the care and management, as in general, prudent men of discretion and intelligence in such matters employ in their own like affairs."92

The doctrine was not altogether a new one. In 1852, the Court of Appeals had held that an assignment for the benefit of creditors was not void by reason of a provision that the trustee was not to be held liable for any loss unless it was caused by his gross negligence or willful misfeasance. The court discussed the various degree of care which different text writers had stated were applicable and then made its own rule by saying:

"The degree of diligence which a trustee uses in his own affairs cannot properly be the subject of judicial inquiry. Every trustee must be presumed by the court before whom his account is taken, to use in his own concerns such dili-

90. In 1900, the Court of Appeals referred with approbation to investments by fiduciaries, who were not restricted to "legals," in the stock of railroad, manufacturing, banking or even business corporations which, by their successful conduct for a long period of time have achieved a standing in commercial circles and acquired the confidence of investors. Matter of Hall, 164 N. Y. 196, 58 N. E. 11 (1900). But for a pessimistic view of stocks as investments for fiduciaries, see Matter of Carnell, 174 Misc. 127, 19 N. Y. S. (2d) 832, aff'd, 260 App. Div. 287, 21 N. Y. S. (2d) 376, aff'd, 284 N. Y. 624, 29 N. E. (2d) 935 (1940).

91. King v. Talbot, 40 N. Y. 76, 84 (1869).

92. Id. at 85, 86.
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gence as is commonly used by all prudent men. (Jones on Bailments, 30). The
diligence of a provident man therefore is the measure of a trustee’s duty.33

One of the reasons why King v. Talbot was accepted so enthusiastically, is that it did not set an impossible standard. It provided that
fiduciaries be tested by comparison with ordinary mortals and not with
supermen. Thus, as one court has stated it, fiduciaries must:
“... be vigilant and prudent, but in the sense in which these qualities are
developed by human beings ordinarily gifted.34

While another said that:
“The measure of duty imposed upon the representative of an estate is not
the highest degree of technical skill or care nor the last word in perfection.”35

One judge made the comforting remark that
“The law does not require infallibility of any trustee.”36

while another, somewhat pessimistically, said that a fiduciary is not
expected:
“... to be infallible in his judgments and decisions. Like all mortals, he is
liable to make mistakes.”37

It should also be noted that if the rule was more stringent, it would
be self-defeating to the extent that the very prudence which the rule
demanded of a fiduciary would keep prudent men from acting as fidu-
ciaries. As one court said:
“It cannot be expected from trustees that they are to act upon principles
different from those which actuate cautious and prudent men in the transac-
tion of their own affairs. Otherwise the office of trustee would be one of such
hazardous responsibility that no prudent or competent men would ever
accept it.”38

93. Litchfield v. White, 7 N. Y. 438, 443. (1852) The court went on to say that other-
wise: “... there would be one rule for a careless, and a different rule for a vigilant
trustee; and the careless trustee would be exonerated in the same case in which the vigilant
would be held liable.” It should be noted that the reverse is now the case. The fiduciary
who, in spite of the exercise of prudence and diligence, retains a security to its loss under
an error of judgment will be exonerated from liability, see note 125 infra; while another
fiduciary who negligently retained the same security for the same period of time
would be held liable.

1934).
96. Atlantic Trust Co. v. Powell, 23 Misc. 289, 293, 50 N. Y. Supp. 866, 869 (Sup.
Ct. N. Y. Co. 1898).
98. Higgins v. Whitson, 20 Barb. 141, 146, 147 (Gen. Term N. Y. Co. 1855); Roose-
Although the rule was promulgated with respect to testamentary trustees, it has been applied to fiduciaries generally, as for example to executors and administrators; to a general guardian; to a committee of an incompetent; and to the trustee of a corporate mortgage. The rule has been made applicable not only to matters involving the purchase and retention of securities but to other matters of fiduciary administration as well, such as the management of real estate and to payment of claims against an estate.

The Negative Rule of King v. Talbot

There is also a negative rule in King v. Talbot, i.e., what a fiduciary must not do. After laying down the rule of the "prudent man," the court went on to say:

"This necessarily excludes all speculation, all investments for an uncertain and doubtful rise in the market, and, of course, everything that does not take into view the nature and object of the trust, and the consequences of a mistake in the selection of the investment to be made.

"It, therefore, does not follow, that, because prudent men may, and often do, conduct their own affairs with the hope of growing rich, and therein take the hazards of adventures, which they deem hopeful, trustees may do the same; the preservation of the fund and the procurement of a just income therefrom are primary objects of the creation of the trust itself, and are to be primarily regarded."

The negative rule in King v. Talbot is of equal importance with the affirmative rule and possibly of easier application. If a fiduciary is in doubt as to the propriety of making or retaining an investment by reason of its type, a recourse to the negative rule will give him an infallible guide. It is not infallible as to the outcome of the proposed investment. Some conservative investments go down; and some specu-

99. Times without number.
105. King v. Talbot, 40 N. Y. 76, 86 (1869). This would make an excellent daily prayer for many fiduciaries.
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lative investments go up. But a fiduciary who follows the negative rule will not only protect himself but will have the satisfaction of knowing that he acted for the best interests of the estate.

While the negative rule has not been cited as frequently as the affirmative rule, it has nevertheless been applied often. It continues to be "the law," perhaps with increasing force and effect.

The Collateral Doctrines to the Rule in King v. Talbot

The courts have established certain doctrines and rules of law with respect to the liability of a fiduciary for the administration of investments which serve to supplement the rule in King v. Talbot without lessening in any respect the degree of care which must be exercised. While the doctrines, on their face, seemingly serve to operate in favor of the fiduciary, they may, nevertheless, be invoked against him.

The more important of these collateral rules are listed here in the order in which they were enunciated by the Court of Appeals, except that the doctrine which pertains only to the retention of securities is for purposes of convenience, placed at the end. They are as follows:

106. Individual situations will naturally arise where the failure of the testator to authorize his fiduciaries to retain common stocks has deprived beneficiaries of their later rise in value. In Matter of Franklin Trust Co., 84 Misc. 686, 147 N. Y. Supp. 838 (Kings Co. 1914), the Court had to rule that a trustee could not retain the stocks of the various Standard Oil subsidiaries which were split up among the stockholders on the dissolution of the parent company. In Matter of Gilma, 39 Misc. 762, 80 N. Y. Supp. 1122 (New York Co. 1903), the executors reported to the court that the testator operated a chain of grocery stores under the name of the Great Atlantic and Pacific Tea Company, together with one Hartford; that the leases were made in the name of the decedent and contracts entered into on his credit but that Hartford claimed, and was suing to establish, an interest in the business; that an offer of settlement had been made whereby the estate would transfer its interest in the business in exchange for a stock interest in a corporation to be formed and requested permission to settle on that basis. The court stated that "... purchases of the stock of a corporation, either domestic or foreign are not favorably regarded." The petition, however, was not denied on that ground but for lack of jurisdiction. The practical outcome of the situation is not known to the writer and the case is referred to only as an example of what might happen.

107. The negative rule has been referred to, not only in cases involving the administration of securities, as for example Matter of Junkersfeld, 244 App. Div. 260, 279 N. Y. Supp. 481 (4th Dep't 1935) and Matter of Yund, 152 Misc. 785, 274 N. Y. Supp. 831 (Montgomery Co. 1934), but where the fiduciary was charged with negligence in allowing claims against an estate, Matter of Saunders, 4 Misc. 28, 23 N. Y. Supp. 829 (Catteraugus Co. 1893); where a depository bank failed, Matter of Watson, 115 App. Div. 310, 100 N. Y. Supp. 993 (1st Dep't 1906); Matter of Scudder, 21 Misc. 179, 186, 47 N. Y. Supp. 101, 106 (Oneida Co. 1897); and in failing to set aside transfers, Matter of Hall, 16 Misc. 174, 175, 38 N. Y. Supp. 1135, 1136 (Catteraugus Co. 1896); for failing to invest in securities, Matter of McNamany, 172 Misc. 392, 393, 15 N. Y. S. (2d) 270, 272 (Kings Co. 1939) Wingate, S.; and in administering real estate, Matter of Hotaling, 250 App. Div. 489, 490, 294 N. Y. Supp. 953, 956 (2d Dep't 1937).
(1) A fiduciary is not a guarantor or insurer for the safety of the securities which are committed to his care.

(2) A fiduciary is not liable for unfortunate results which he could not foresee and is unable to prevent.

(3) A fiduciary should be judged in the light of the facts as they existed at the time of their occurrence.

(4) A fiduciary who acts in good faith and employs the care and diligence demanded of him is not responsible for errors of judgment.

(5) A fiduciary is not responsible for losses arising out of investments which he did not make, if he exercises due care and prudence in disposing of or retaining them.

_A Fiduciary Is Not a Guarantor or Insurer for the Safety of the Securities Which Are Committed to His Care_

In 1878, Judge Speir of the Supreme Court of New York County decided the comparatively little known case of _Roosevelt v. Roosevelt_, 108 and in so doing, wrote an opinion which incorporated in whole or in part doctrines which were subsequently adopted by the Court of Appeals in three different cases. 109 The issue involved the liability of a fiduciary for making a mortgage investment which resulted in a loss. The proof showed that the mortgage was acquired with the exercise of proper care, that the property value was substantially in excess of the mortgage loan when made, and that the loss was caused by a general decline in real estate values. In holding that the trustee was not liable, Judge Spier said:

"... when one has faithfully endeavored to execute a trust, it would be both unreasonable and inequitable to make him an insurer against losses from casualties and misfortunes which ordinary sagacity could not prevent." 110

Three years later, the Court of Appeals decided _McCabe v. Fowler_, 111 which involved the liability of an executor for the loss of estate securities which had been stolen by the person in whose custody the executor had left them. In holding on the facts involved that the fiduciary was not negligent and hence not responsible for the loss sustained, the court laid down the doctrine that:

"An executor or trustee is not a guarantor for the safety of the securities

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111. McCabe v. Fowler, 84 N. Y. 314, 318 (1881).
which are committed to his care, and does not warrant such safety under any and all circumstances, and against all contingencies, accidents or misfortunes."

The court then stated the rule of *King v. Talbot* and added:

"While this rule requires an executor or trustee to avoid all extraordinary risks in the investment of the moneys of the estate and to keep the same safely, it does not demand that he be made liable for contingencies which under ordinary circumstances, could not have been anticipated."

The rule will operate in favor of fiduciaries who have been prudent and diligent and who were not personally responsible for the losses complained of, such as where an attempt was made to hold one fiduciary liable for funds embezzled by his co-fiduciary; where the attorney for a fiduciary stole securities from her by sleight-of-hand methods which they were being examined in a safe-deposit vault; where the losses were due to a general decline in values; and where a fiduciary had distributed an estate in good faith at the end of the statutory period of administration, relying upon affidavits and statements as to who were the next of kin and was called upon to face the claims of a relative who subsequently appeared.

While the doctrine is a shield for the diligent and careful fiduciary, it may be used also as a sword against the fiduciary who has been remiss in the performance of his obligations to his trust estate. The doctrine was no protection to the fiduciary who invested in wild-cat oil stocks, or to the executor who retained common stocks without authority to do so and without jurisdiction for its action until their values totally disappeared, or to the guardian who entrusted to his attorney the matter

112. Id. at 315.
115. Matter of Juilliard, 171 Misc. 661, 665, 1 N. Y. S. (2d) 315, 318 (Orange Co. 1939) Taylor, S. The court said a fiduciary should not be required to determine in every case at his peril the mental competency of his associate.
118. Matter of Cady, 211 App. Div. 373, 375, 207 N. Y. Supp. 385, 387 (4th Dep't 1925). The court, speaking of a trustee, said: "While he is not a guarantor of the safety of the securities in his charge belonging to the estate, he is bound to exercise such prudence and diligence in the care and management of the estate as men of discretion and intelligence in general employ in their own affairs."
of investing the estate funds and the attorney stole them, since the loss was made possible by an unauthorized delegation of power.\textsuperscript{120}

\textit{A Fiduciary Is Not Liable for Unforeseen Results which He Could Not Foresee and Is Unable to Prevent}

Simultaneously with its holding that a fiduciary was not a guarantor,\textsuperscript{121} the Court of Appeals passed upon the liability of an executor who was charged with negligence in failing to foreclose a mortgage which had been an investment of the testator. The executor defended his course of conduct on the ground that there had been a general decline in real estate values. The Court refused to hold him liable, saying of a fiduciary that:

"... and while no rule of proper responsibility should be relaxed, yet where he acts honestly and in good faith, and with reasonable prudence and discretion, he should not be held liable for unfortunate results which he could not be expected to foresee and was powerless to prevent."\textsuperscript{122}

The reasons for the rule were given in greater detail a few years later in a case involving the liability of a fiduciary for investing in mortgages which depreciated in value with a decline in real estate. The court said:

"If the defendants acted in good-faith in making these loans, subsequent events which they could not foresee and over which they had no control, operating to deprecate the value of these securities, would not render them liable to make good such loss to the estate. Such a rule would require a trustee to forecast the future with invariable accuracy, and in case of failure to do so, make him responsible for the consequences, even though he exercised the greatest caution and prudence in making investment. Under such a rule no prudent man would or could safely undertake the management of a trust estate, and it would be difficult to obtain honest and reliable men to accept what is a very necessary though is often a thankless and troublesome duty."\textsuperscript{123}

The doctrine was re-phrased in a later case, when the court, in refusing to surcharge a fiduciary, uttered the comforting words that "the law does not require infallibility of any trustee."\textsuperscript{124}

\begin{footnotes}
\item[120] Matter of Pinchefski, 179 App. Div. 578, 166 N. Y. Supp. 204 (3d Dep't 1917).
\item[121] McCabe v. Fowler, 84 N. Y. 314 (1881).
\item[122] Ormiston v. Olcott, 84 N. Y. 339 (1881) (italics added).
\item[123] Crabb v. Young, 92 N. Y. 56, 68 (1883).
\end{footnotes}
A Fiduciary Should Be Judged in the Light of the Facts as They Existed at the Time of Their Occurrence

In 1895, the Court of Appeals was called upon to decide if two fiduciaries should be held responsible for the actions of a third trustee who was unable to account for funds which they had permitted him to hold. In ruling that the two innocent fiduciaries had been justified in allowing their colleagues to handle the fund in question and had not been negligent in failing to suspect him of any wrong-doing at the time, the court said that:

"We are to look at the facts as they exist at the time of their occurrence, not aided or enlightened by those which subsequently take place by reason of which the loss has occurred."125

The Court of Appeals lay down the same doctrine fifteen years later in a case involving the liability of certain trustees when it said that:

"... a wisdom developed after the event and having it and its consequence as a source is a standard no man should be judged by."126

A Fiduciary Who Acts in Good Faith and Employs the Degree of Care, Prudence, and Diligence Demanded of Him Is Not Responsible for Errors of Judgment

In 1913, the Court of Appeals handed down an opinion which simultaneously re-enacted the rule in King v. Talbot and added an amendment to it. In dealing with the liability of a trustee, it said:

"The statutory provision and the rules of equity characterizing the securities in which trust funds may be invested were adopted in the light of experience and we do not intend to weaken them or increase their elasticity. They are not, however, absolutely exclusive, arbitrary and inflexible and must yield to the rule of necessity or safety. A more fundamental and broader principle, superseding in emergencies or justifying conditions the specialized rule, is that trustees are bound in the management of all the matters of the trust to act in good faith and employ such vigilance, sagacity, diligence and prudence as in general prudent men of discretion and intelligence in like matters employ in their own affairs. The law does not hold a trustee, acting in accord with such rule, responsible for errors in judgment. Matter of Denton v. Stanford,

126. Costello v. Costello, 209 N. Y. 252, 262, 103 N. E. 143 (1913). The natural honesty of this doctrine must be abhorrent to the "liberal" judge who has no compunction about changing settled rules of law and applying the new doctrines to completed transactions in order to satisfy his personal ideologies."
The doctrine has been cited on innumerable occasions, generally in opinions in which the fiduciary was freed from responsibility for losses sustained by the trust estate.

It is well to remember, however, that the decision does not grant a general amnesty to all fiduciaries who guessed wrong. Before a fiduciary can plead "errors of judgment" as a defense, he must first establish that he has conformed to the doctrine of King v. Talbot. If he cannot, then "errors of judgment" are not a defense.

A Fiduciary Is Not Responsible for Losses Arising out of Investments which He Did Not Make if He Exercises Due Care and Prudence in Disposing of or Retaining Them

In 1883, the Court of Appeals passed upon the responsibility of executors who retained for over a year 1,500 shares of a speculative railroad stock which dropped from 80 to 15. The court found that the fiduciaries had been diligent and careful in administering the securities and refused to surcharge them. Among the reasons given was the fact that:

"... the executors did not make this investment. They found the stock among the assets. Without their fault it came into their hands and they had to care for and dispose of it, with all its inherent risks on the one hand and possibilities on the other."128

The doctrine was also phrased by Judge Cardozo a number of years later in a more guarded manner, when he said:

"Support is not lacking altogether for the view that the duty to call in an investment no longer appropriate, is not always co-extensive with the liability growing out of an investment unlawful in its origin."129

The reasons for the rule were explained later by the Appellate Division of the Second Department when it said:

"In the one case, the investment, whether wise or unwise, is the independent, uncontrollable act of the owner; and in the other it is the act of the trustees whose discretion is often limited and whose duties are generally prescribed either by the will or statute; and each is to be subjected therefore, to wholly different rules, if indeed, the act of the owner is subject to any rule whatsoever."130

The doctrine was applied in its fullest effect in Matter of Clarke\textsuperscript{131} which is not only a leading case but one which deserves particular mention if for no other reason than that it seems to be misunderstood. The facts were simple. A trustee had received from the estate of a testator stocks of a sugar company, investments which the testator himself had made. The stocks were speculative in their nature and the market was declining. The trustees sought the advice of leaders in the sugar industry as to whether to hold or to sell. It was advised to retain the shares and it did so. When it accounted, it was surcharged by the Surrogate for a loss which had been sustained and the surcharge was affirmed by the Appellate Division. The Court of Appeals reversed and in so doing assembled doctrines already well established and set them forth, without adding anything new, as a restatement of the law as to the obligations of fiduciaries in the administration of investments. It laid down:

\begin{itemize}
\item[a] The rule of prudence and diligence from King v. Talbot.\textsuperscript{132}
\item[b] The rule that the court must look at the facts as they existed at the time of their occurrence, from Purdy v. Lynch.\textsuperscript{133}
\item[c] The rule that a fiduciary is not to be judged by wisdom acquired after the event, from Costello v. Costello.\textsuperscript{134}
\item[d] The rule that there was a difference in the degree of liability with respect to the retention of an investment made by the testator, and the retention of an investment made by the fiduciary, from Matter of Weston.\textsuperscript{135}
\item[e] The rule that fiduciaries who comply with the standards of conduct imposed on them are not liable for errors of judgment—and here, the court cited not its own decision to that effect in Costello v. Costello but Matter of Chapman an English decision.\textsuperscript{136}
\item[f] The rule that fiduciaries are not liable for results which could neither be foreseen nor prevented, from Ormiston v. Olcott.\textsuperscript{137}
\end{itemize}

Matter of Clarke is a good decision and no criticism can be found with it. But there seems to be a tendency to apply it to investments made by a fiduciary, whereas on its facts, it is operative only with respect to the retention of securities which the testator, not the trustee, had purchased. The court could not have made this more evident. It said:

\begin{itemize}
\item[132] King v. Talbot, 40 N. Y. 76 (1869).
\item[133] Purdy v. Lynch, 145 N. Y. 462, 40 N. E. 232 (1895).
\item[134] Costello v. Costello, 209 N. Y. 252, 103 N. E. 148 (1913).
\item[135] Matter of Weston, 91 N. Y. 502 (1883).
\item[136] Matter of Chapman, 2 Ch. 763, 767 (1896).
\item[137] Ormiston v. Olcott. S4 N. Y. 339 (1881).
\end{itemize}
“Self-evidently, the purchase of a speculative stock of a trustee is one thing; the retention of such a stock awaiting the arrival of a favorable opportunity to sell is quite another; the former would constitute negligence; the latter, regarded prospectively, might be prudent although in retrospect it might seem to have been a grievous error of judgment.”

On its facts, therefore, *Matter of Clarke* does not afford protection to a fiduciary whose investment administration is under attack unless the following factors are present:

1—That the investment was one made by the decedent.
2—That the retention was due to the lack of a favorable opportunity to sell. This will exclude a situation where a speculative stock is held during a period when it could have been sold without loss, and thereafter depreciate.
3—Possibly, that the fiduciary had the right of retention. But if the stock comes into the hands of the fiduciary in time of stress, this may be relatively immaterial.

It should also be remembered that the corporate fiduciary in *Matter of Clarke* had been extremely diligent in determining what action to take. If it had been left merely to a routine administration, *via* the committee system, it is quite possible that the trust company would not have been exonerated.

The doctrine that a distinction should be made between investments which a fiduciary receives, and those which he makes, became so strongly established that it was eventually enacted as a statute. Subdivision 6 of Section 111 of the Decedent Estate Law, provides as follows:

“No fiduciary shall be liable for any loss incurred with respect to any investment not eligible by law for the investment of trust funds if such ineligible investment was received by such fiduciary pursuant to the terms of the will, deed, decree of court, or other instrument creating the fiduciary relationship or if such ineligible investment was eligible when received, or when the investment was made by the fiduciary; provided such fiduciary exercises due care and prudence in the disposition or retention of any such ineligible investment.” 138

**The Liability of a Fiduciary in Connection with the Making of a Legal Investment**

There seems to be some conflict of opinion as to the liability of a fiduciary in connection with the making of an investment permitted by statute. The earlier decisions held without qualification that a fiduciary was obliged to exercise care, prudence and diligence in making legal...
as well as non-legal investments. Thus, in 1911, Surrogate Fowler surcharged a trustee for making a mortgage loan because, although the loan did not exceed two-thirds of the value of the property, the fiduciary had failed to take into consideration the financial circumstances of the mortgagor. Surrogate Fowler stated that the mathematical qualifications for the mortgage loan which were qualifications fixed by law were not sufficient in themselves but were

"... always coupled with the implied proviso that such loan is to be in other respects reasonable and proper. The surrogate does not understand that this qualification, formerly well known in Courts of Chancery, is abrogated by the statutes of either England or New York regulating pro tanto the investments of trustees. On the contrary, this qualification must be read, as it were, into the statutes."\textsuperscript{139}

The same rule was adopted with respect to investments in guaranteed mortgage participations. In 1933, Surrogate Wingate said that:

"Indeed, it has been authoritatively determined that the statutory authorization furnishes a potent protection for an investment only where its making is a prudent and otherwise proper act."\textsuperscript{140}

And shortly afterward, Surrogate Delehanty decided \textit{Matter of Frazer}, where he said:

"Nor has the court ruled that merely because an investment falls within the category of 'legals' a fiduciary may rely upon that fact alone to justify the investment. The rule in \textit{King v. Talbot}, 40 N. Y. 76, is still the rule of liability for fiduciaries.... Even when the investment is made in a security authorized by law, a fiduciary must be prepared to meet proof that in the particular instance the investment was improper, imprudent and unreasonable."\textsuperscript{141}

This was followed by \textit{Matter of Jacobs}, in which the court held expressly that the making of an investment permitted by statute:

"Does not absolve the trustee entirely from exercising sound judgment and due discretion in making the investment."\textsuperscript{142}


\textsuperscript{140} Matter of Sarah Blake, 146 Misc. 780, 782, 263 N. Y. Supp. 310, 313 (Kings Co. 1933) Wingate, S.

\textsuperscript{141} Matter of Frazer, 150 Misc. 43, 50, 268 N. Y. Supp. 477, 485 (New York Co. 1933) Delehanty, S.

\textsuperscript{142} Matter of Jacobs, 152 Misc. 139, 142, 273 N. Y. Supp. 279, 282 (Delaware Co. 1934) O'Conner, S.
The doctrine was followed by the Appellate Division in *Matter of Flint* when it said that a corporate fiduciary, not limited to legal investments, which nevertheless had invested in them, was not absolved:

"... from the rule that it must exercise prudence, foresight and good faith, and refrain from negligent acts of commission or omission."^{143}

The Court of Appeals spoke on the subject in January 1936. In deciding a case which did not directly involve the liability of a fiduciary for investment but a collateral question, the court said:

"The fiduciary who invests in securities within the specified classes is not by the statutes freed from liability for resultant damages if he fails to exercise reasonable judgment and discretion in making the investment."^{144}

In the same year, Surrogate Delehanty handed down an opinion in the leading case of *Matter of Dalsimer* in which he surcharged a fiduciary who had invested in a "legal" mortgage participation, stating that a fiduciary continued under the obligation of exercising care, diligence and prudence, even though the investment came within the statute. The decision was squarely upheld on appeal by the Appellate Division of the First Department, the court saying that subdivision 7 of Section 188 of the Banking Law:

"... leaves untouched the established general rules of law regarding the care and fidelity of one acting in a fiduciary capacity and the obligation that a trustee must act with prudence, foresight and vigilance and without negligence in making trust fund investments."^{145}

The opinion could not have been more definite on the subject. Judge Dore said:

"But a fiduciary who invests in securities within the classes specified by statute [Decedent Estate Law § 111] is not free from liability for resultant loss if he fails to exercise reasonable judgment and discretion in making the investment. (Delafield v. Barret, 270 N. Y. 43, 48; Matter of Jacobs, 152 Misc. 139; Matter of Randolph, 134 N. Y. S. 1117, affd. 150 App. Div. 902; appeal dismissed, 207 N. Y. 685).

"A trustee by acceptance of the office assumes the duty of satisfying himself with reasonable care of the soundness of an investment at the time it is made and cannot merely or principally rely on the guarantee of a title company but must rely primarily on the real security which the law requires of

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an investment of this character and then the guarantee may afford added security."146

In January, 1937, the Appellate Division of the Second Department reaffirmed what it had said in Matter of Flint, that the statutes regulating investments by corporate fiduciaries "leave untouched the obligation of a trustee to act with prudence, foresight and vigilance and without negligence in making investments."147

Up to this point, there had been practically no questioning of the rule that the liability of a fiduciary for care, prudence and diligence applied to the making of legal investments.148 But in 1937, the Court of Appeals decided Mills v. Bluestein,149 and in so doing, opened up the question, either entirely or partly, for reconsideration. The case involved the liability of the Chamberlain of the City of New York, who, pursuant to a court order, had purchased as an investment for a fund a guaranteed mortgage participation which was prima facie, a legal investment. The official made no independent investigation as to encumbrances on, or as to the value of, the mortgaged property, relying exclusively on the guaranty and assurance of the mortgage company that the participation was a legal investment. It later appeared that there were unpaid taxes on the property when the investment was made and it was found that the loan exceeded two-thirds of the value of the property. The Court of Appeals held that the responsibility of the Chamberlain was similar to that of a trustee, and that hence he was obligated to exercise the same care and prudence which a reasonable man would exercise in the management of his own affairs, but found on the facts that he was not negligent.

Some of the reasons advanced by the court were of general application. Thus, in speaking of the tax arrears, the court said:

"Even a trustee is not to be charged with moneys invested by him in good faith in securities which do not fully meet the standard prescribed by the statutes for the investment of trust funds where failure to discover the defect is not due to negligence or other fault of the trustee."150

And it pointed out that the Chamberlain had relied upon assurances as to the investment which were made by a company functioning under the supervision of the Insurance Department of the State; that an in-

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146. Id. at 360, 296 N. Y. Supp. at 215.
150. Id. at 323, 9 N. E. (2d) at 946.
vestor might reasonably assume that the representations were made in
good faith and after proper investigation; that in 1929, when the in-
vestment was made, the solvency and stability of the guarantor was not
challenged and that it could not be said that prudence dictated that the
representation or assurance of the guaranteeing company should be for-
tified by another title search or appraisal. But some of the reasons
were pertinent only with respect to the particular fiduciary before the
court when it said:

"The city chamberlain could hardly be expected to search the title or ap-
praise the value of every parcel of real estate subject to a mortgage in which
court funds are invested. To do so in person would be a physical impossi-
bility, and he has no staff of deputies who can do so in his place. All that
can be required of him is to make such investigation and to obtain such in-
formation as would under the circumstances seem sufficient to a reasonably
prudent investor."\(^{151}\)

The reasons advanced which relate to the Chamberlain's lack of inves-
tigating facilities may be advanced also with respect to the individual
fiduciary but obviously do not apply in their entirety to corporate fidu-
ciaries. Consequently, there is doubt as to the extent to which Mills v.
Bluestein protects a corporate fiduciary, particularly because nine
months later, the Court of Appeals affirmed, without opinion, Matter
of Dalsimer.

But the situation again became complicated when, on January 10,
1939, the Court of Appeals decided Matter of Smith\(^{152}\) which involved
an investment by the committee of an incompetent war veteran in a
guaranteed mortgage participation. The committee was the sister of
the incompetent and the investments had been made pursuant to court
orders which had been obtained by the Veterans Administration, facts
which established at least good faith in the making of the investment.
After holding that the investment as such was proper for the committee
of an incompetent, the court discussed the further objections made that
the mortgaged property was subject to tax liens and not worth more
than 50% more than the amount of the loan. In refusing to surcharge
the committee for the investment, in spite of these defects, the court
said:

"Only a title search and an appraisal of the mortgaged premises would have
disclosed such infirmities in the investment. A fiduciary may not escape lia-

151. Id. at 323, 324, 9 N. E. (2d) at 946.
his peril when he disregards statutory limitations upon his power. \((DeCaf
dfield v. Barret, supra.\) He may not, however, be charged with wrong and
liability for consequent damage, when in spite of the exercise of care and
prudence he fails to discover extraneous facts which render a particular in-
vestment—though of the type sanctioned by the statute—unsafe and im-
proper for trust funds. In this case the committee appears to have used the
care and prudence which a reasonably careful committee would under the
circumstances have used \((Mills v. Bluestein, 275 N. Y. 317).\)\(^{153}\)

The courts have not been unanimous in their interpretation of the
decisions in \(Mills v. Bluestein\) and in \(Matter of Smith,\) and the ques-
tion still remains open as to how broadly or how narrowly their hold-
ings should be applied. The decisions of the lower court and of the
Appellate Division of the Second Department in \(Cobb v. Gramatan
National Bank,\)\(^{154}\) illustrate this to some extent. Here, almost every fact
served to make the fiduciary liable. In 1926, a mortgage of \$25,000
had been placed upon a private residence. The mortgage was foreclosed
in 1930. The guarantor bought it in at the foreclosure sale for
\$20,000 and resold it for \$25,000 no part of which was paid in
cash; the entire consideration being a purchase money mortgage for
\$25,000. The purchaser-mortgagor was a corporation which had been
organized for the purpose of taking title to the property and had
no other assets. The title company guaranteed the \$25,000 purchase
money mortgage and sold it to the fiduciary. The lower court
found that when the investment was made, the property had been va-
cant for more than a year and that current taxes were in default. It
said, and it does not appear to be disputed, that:

"Not the slightest investigation or inquiry was made by the trustee in con-
nection with the investment. The title company was not asked who owned
the property, who occupied it, what it was assessed for, what its condition was
or at what value it was appraised. The trustee relied wholly upon the assurance of the title company that its mortgage certificates generally met the
standard prescribed. .."\(^{155}\)

In discussing the extent to which the fiduciary was relieved by the de-
cision in \(Mills v. Bluestein\) from the responsibility of making an inde-
pendent investigation, of the mortgaged property, the lower court said:

"If the trustee had done anything at all to assure itself that this investment
was a proper one for trust funds, even if it had relied upon information fur-
nished to it by the title company which turned out to be false, it might be

\(^{153}\) Id. at 489.

Westchester Co. 1940), aff'd, 261 App. Div. 1086, 26 N. Y. S. (2d) 917 (2d Dep't 1941).

\(^{155}\) Id. at 50.
said to have exercised reasonable care. But how can it be said that it exercised reasonable care when it did nothing at all.\footnote{156}

The opinion further distinguished \textit{Mills v. Bluestein} on the ground that the mortgage investment which was there involved had been made in 1929 whereas this mortgage investment was made in 1931. Thus, the lower court refused to relieve the fiduciary from liability merely on the ground that it was entitled to rely on the fact that the mortgage was guaranteed, and surcharged it, despite anything in \textit{Mills v. Bluestein} to the contrary. The Appellate Division affirmed but in a memorandum opinion which left its reasons in doubt. The opinion said in part that:

"... the character of the investment here is not seriously defended. The making of it is sought to be justified on the ground that the trustee had a right, as a matter of law, to rest on the assurances and representations of the title company with which it dealt. These grounds of justification do not touch the breach of duty by the trustee in respect of making the investment of such a large sum, representing the entire corpus of the trust fund, in a single security. The trustee in doing so was grossly negligent as a matter of fact and as a matter of law. An additional finding of fact and conclusion of law to this effect will be made."\footnote{157}

There was a strong dissent on the ground that under \textit{Mills v. Bluestein} and \textit{Matter of Smith}, the fiduciary did not have to make an independent investigation.\footnote{158} The failure of the majority opinion to rule directly on this point and its sudden injection of lack of diversification makes it arguable as to whether there would have been an affirmation if the factor of diversification had not been present. The situation is not clarified by the fact that the lower court held that \textit{Mills v. Bluestein} and \textit{Matter of Smith} were distinguishable on the facts and hence not applicable. The majority opinion in the Appellate Division did not even mention them and the dissenting opinion held them to be completely controlling. But even if \textit{Mills v. Bluestein} and \textit{Matter of Smith} have not the wide latitude suggested in the dissent, their effect has naturally been to relieve fiduciaries from liability from losses on guaranteed mortgages or participations therein, if the facts show some degree of independent investigation by the fiduciary. Thus, when there was ample evidence of prudent investigation and inspection preliminary to the placing of the mortgage, the court, in refusing to surcharge a fiduciary,

\footnote{156} \textit{Ibid.}
\footnote{157} \textit{Id.} 261 App. Div. at 1086, 26 N. Y. S. (2d) at 917.
\footnote{158} \textit{Id.} 261 App. Div. at 1087, 26 N. Y. S. (2d) at 918. Other cases cited were \textit{Matter of Stupack}, 274 N. Y. 198, 8 N. E. (2d) 485 (1937), and \textit{Matter of People v. Title Mortgage Guarantee Co.}, 264 N. Y. 69, 190 N. E. 153 (1934).
referred to the "trend" of these decisions, while another court cited *Mills v. Bluestein* as authority for the doctrine that a fiduciary was not negligent in relying upon a representation of a guarantor sanctioned by the Insurance Department of the State.

But *Mills v. Bluestein* and *Matter of Smith* cannot be extended unduly. Thus when a fiduciary who was limited to mortgages which did not exceed 60% of the value of the property invested estate funds in guaranteed mortgage certificates, the court surcharged him with respect to loans in excess of 60% of the value of the property, saying:

"Authorities for the holding that, generally trustees might safely invest in mortgage certificates and rely on the guarantee without being fortified by an independent search and appraisal, such as *Mills v. Bluestein*, supra, have no application here, where the limitation prohibits the making of mortgage loans in excess of 60% of the value of the property."

In another instance, a court surcharged an individual trustee who had purchased a guaranteed mortgage when it appeared that the slightest investigation would have disclosed its unsuitability, applying the doctrine laid down in *Matter of Dalsimer* that the trustee could not rely merely or principally upon the guarantee but must rely primarily on the real security which the law required for an investment of the character involved and in a recent case, the court surcharged a fiduciary for failing to investigate the rentals of the mortgaged properties which were insufficient to pay the interest and carrying charges, and relying instead upon the guarantee. The court said:

"... and if the mortgaged property be regarded as the primary security for the payment of the debt, the income therefrom is the primary security for the payment of the mortgage interest, among other charges, until the payment of the debt."

It is hardly necessary to state, however, that the courts have recog-
nized that reliance upon representations of a guarantor of a mortgage is not *per se* forbidden. Thus, when an attempt was made to surcharge a fiduciary for investing in a guaranteed mortgage and it appeared that the trustee was himself familiar with real estate values and was thoroughly experienced in the mortgage investment field, he was exonerated from liability, the court saying:

"If in addition, he gave consideration to the representations of a company in good standing with whose officers he was acquainted, and whose judgment he respected, he is not for that reason alone to be surcharged."

On principal, it would seem that universal application might well be given to the ruling laid down by *Mills v. Bluestein* and *Matter of Smith* that a fiduciary may rely upon assurances and representations of a guarantor as to all matters affecting title to the mortgaged premises, for it would be unreasonable to require a fiduciary to pay for both a guaranty and an independent title search, and obviously it could not search the title itself.

But a different situation exists with respect to the factor of value. It is suggested that the character of the particular fiduciary involved should constitute a factor of major and perhaps determining importance. It may well be that a city official or the relative of an incompetent or any individual fiduciary who does a careful and conscientious job, should not be surcharged for having failed to make a detailed investigation into the value of the property upon which he had obtained a guaranteed mortgage. But it does not follow that corporate fiduciaries should be granted the same privileges. They have officers whose business it is to be familiar with real estate values. They function as fiduciaries on a professional basis and they advertise their qualifications as such. It would seem, therefore, that they should be held to a higher degree of care and should be required to make their own examination and investigation of properties before investing estate funds in mortgages upon them. Hence it is suggested that as to the factor of value, they should be bound by the rule of *Matter of Dalsimer* rather than by the rule of *Mills v. Bluestein* and *Matter of Smith* and that they should be protected by the assurances and representations of the guarantor as to value only to the extent that they serve to supplement and corroborate their own opinions and appraisals independently arrived at.

With respect to the current earnings of a mortgaged property, every fiduciary, whether individual or corporate is expected to be able to add and subtract, and hence every fiduciary should be obligated to look at an earning statement, total the receipts and expenses, deduct the latter from the former and see if the result is plus or minus.

[To Be Continued]