TRUSTS - INVESTMENT OF TRUST FUNDS IN THE SECURITIES OF PRIVATE CORPORATIONS

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TRUSTS — INVESTMENT OF TRUST FUNDS IN THE SECURITIES OF PRIVATE CORPORATIONS — The trustees of a charitable trust established for the erection and maintenance of a hospital sued the state attorney general as a representative of an unnamed class of beneficiaries to secure the approval of certain investments of the trust fund. The transactions in question were investments in the common and preferred stocks of private corporations. Held, the trustees had authority to invest in the common and preferred stocks of private corporations provided they exercised a reasonable degree of care under the circumstances. Rand v. McKittrick, (Mo. 1940) 142 S. W. (2d) 29.

Three factors may limit the classes of investments that a trustee can make without the danger of being surcharged with losses: (1) the terms of the trust indenture; (2) statutory regulations; (3) judicial decisions. The settlor by the trust instrument can, and commonly does, grant the trustee a broader field of investment than is allowed by either the statutes or judicial decisions. The trustee can purchase any securities within the granted field with impunity, provided reasonable care is used. If the trust instrument makes no provision pertaining to investments, then the trustee must look to local statutes to determine the scope of his authority. Thirty-two states have statutes with lists of classes of "legals" or permissible investments. A majority of the statutes are permissive in form. Under this type of statute, the trustee can make nonlisted investments but he thereby loses the presumption of due care. The rest of the

4 States without such lists include: Arizona, Connecticut, Kansas, Maine, Massachusetts, Michigan, Mississippi, Missouri, Montana, Nevada, New Hampshire, New Mexico, Rhode Island, South Dakota, Utah, and Vermont.

Though the statutes may be permissive in form, some of the courts may interpret them to be mandatory as the New York court did in the case of In re Doegler's Estate, 254 App. Div. 178, 4 N. Y. S. (2d) 334 (1938). The court in that case said that the trustee must invest funds in securities authorized by the statute.

6 In re Cook's Trust Estate, 20 Del. Ch. 123, 171 A. 730 (1934).
statutes are mandatory in form, that is, the trustee must, at the risk of personal liability for losses, invest in listed securities. The statutes in their lists uniformly allow investments in United States bonds, state and local government bonds and first mortgages on real estate. Some extend the lists to include the securities of public utility corporations which meet required standards. Four states specifically permit investments in the stock of private corporations. On the other hand, the constitutions of four states, as well as some statutes, specifically forbid such investments. In the absence of legislation authorizing the purchase of corporate stocks, the numerical weight of authority holds that as a matter of law the trustee making such investments is surcharged with any resulting losses. The minority view followed by Missouri in the principal case holds that the validity of such investments depends upon whether the particular purchase was reasonable. This view results in a desirable flexibility in investment policy for the trustee and also increases the income possibilities for the trust. But the protection given the beneficiary by the test of reasonableness does not seem as satisfactory as that afforded by investment standards established by the legislature. Despite the relative rigidity of the latter, the protection furnished the beneficiary and the certainty given the trustee make it more desirable as a matter of general public policy, especially in view of the fact that any desired variations can be made by the parties in the terms of the trust indenture.

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9 Most statutes require government bonds to meet certain qualifications in regard to record of payments and financial status.
11 Idaho, Kentucky, Oregon. See statutes in notes 5 and 7. See also N. J. Rev. Stat. (Supp. 1939), § 3:16-1. Most of these statutes require the stocks to meet certain qualifications; for example, Oregon requires them to be listed on the New York Stock Exchange.
12 Ala. Const. (1901), § 74; Colo. Const. (1876), art. 5, § 36; Mont. Const. (1889), art. 5, § 37; Pa. Const. (1874), art. 3, § 22.
13 Cal. Gen. Laws (Deering, 1937), Act 652, § 37. This deals with bank investments but also applies to investments by trust companies.
14 King v. Talbot, 40 N. Y. 76 (1869); Clark v. Clark, 167 Ga. 1, 144 S. E. 788 (1928); Sellers v. Milford, 101 Ind. App. 590, 198 N. E. 456 (1936).
15 Harvard College v. Armory, 9 Pick. (26 Mass.) 446 (1930); In re Buhl's Estate, 211 Mich. 124, 178 N. W. 651 (1920). In general, see annotations, 12 A. L. R. 574 (1921); 122 A. L. R. 577 (1939).
17 White and Lawres, "The Modernization of Legal Lists," 5 Law & Contem. Prob. 386 (1938). The authors suggest another solution to the problem of trust investments—to form a board with broad discretionary powers to select suitable securities for trust investments. See also 49 Yale L. J. 891 (1940).
18 See note 2, supra.