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Comment

PRUDENT MAN INVESTMENT OF TRUST FUNDS DURING INFLATION

Hardship has overtaken the income beneficiaries of many trusts which, when created, were thought to provide adequate support. A steadily mounting cost of living,[1] product of an inflation which may continue for an indefinite period, combined with other factors,[2] has greatly reduced their purchasing power. Hardest hit have been beneficiaries who depend on income from small trusts, trusts with restrictive investment clauses, trusts governed by legal lists and trusts managed under extremely conservative investment practices. Consider the problem of a widow, the income bene-

[1] The Federal Reserve Consumers Price Index (based on B.L.S. data) at year end 1950 was 178.4 compared to the 1940 level of 100.2 (base 1935–39 = 100). The dollar had thus depreciated in value to roughly 56¢ in terms of 1940 purchasing power. The Wholesale Commodity Price Index (a measure of general price level) had risen from 77.1 in 1939 to 183.6 in February of 1951, a rise of 138%, 37 FED. RES. BULL. 444, 445 (1951).

[2] Highest grade corporate bond yields have steadily decreased from 5% highs of the twenties to a range of 2.5-2.8% during the forties, and are currently showing slight improvement from their 1950 average of 2.62%. (MOODY'S INVESTOR SERVICE.)

Government issues of fifteen year maturities lately have yielded up to 2.47%. Tax exempt municipals yielded an average of 1.87% in March, 1951. (STANDARD AND POORS.)

These low yields are due chiefly to the government's fiscal program, largely dominated by the huge debt outstanding. See Miller, *Reconciling Monetary Management and Debt Management Policies,* 5 JOUR. OF FIN. 368 (1950); *Recent Monetary and Credit Developments,* 36 FED. RES. BULL. 1275 (1950).

The increases in income taxes during the past ten years have also taken substantial bites from once exempt trust incomes.

ficiary of a $100,000 trust created in 1939, remainder over to grown children or to a charitable institution. Invested in accord with the legal list then prevailing, income in 1939 and 1940 was approximately $2,850 annually.[3] In 1950, that same type of portfolio yielded $2,650, but was worth only $1,540 in terms of 1939 purchasing power. In order to maintain the same purchasing power in 1950, the portfolio would have had to earn $4,900 net, or approximately $5,800 before taxes. Since the better grade corporate bonds were yielding approximately 2.65% and government bonds 2.5% and lower, this return (5.8%) would have been impossible with the usual legal list portfolio.[4] Assuming that only one-third of the fund was invested in common stock in 1950, and that the stock yielded 6%, the trust income would have been approximately $3,200 after taxes. Such a diversification, although an improvement, still would have provided an inadequate income.

The remaindermen fare little better. Although the same number of dollars may be maintained and distributed to them, it is obvious there has been a substantial detrimental change where the dollar has depreciated more than 40% in value.[5] The investment objectives of the income beneficiaries and remaindermen are not entirely inconsistent, at least as far as the common enemy inflation is concerned.

California's Prudent Man Rule

Before examining the possibilities of minimizing the effect of inflation by making particular trust investments, the applicable law governing permissible investments must be sought. California has tried both of the recognized systems of trust investment control: the legal list and, since 1943, the prudent man rule. Absent an investment clause in the trust instrument prescribing a different standard, California trustees are governed by Section 2261 of the Civil Code which embodies the Model Prudent Man Statute.[6] It provides that:

> (1) In investing, . . . a trustee shall exercise the judgment and care, under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of their capital. Within the limitations of the foregoing standard, and subject to any express provisions or limitations contained in any particular trust

[3] No income tax would have been payable on this amount in 1939.

[4] 37 FED. RES. BULL. 422 (1951).

[5] "The principal of a bond portfolio is obviously not safe in real terms if there is any reasonable prospect that the value of the monetary unit will be subject to depreciation." Hayes, *Common Stocks and Safety of Principal*, 5 JOUR. OF FIN. 387 (1950).

[6] Subsection 1 is taken almost exactly from the model statute drafted by the Committee on Fiduciary Legislation of the Trust Division of the American Bankers Association, which is substantially verbatim from the opinion of Justice Putnam in Harvard College v. Amory, 9 Pick. 446 (Mass. 1830), generally regarded as the foundation of the rule. Subsection 5 makes Section 2261 apply to all existing trusts as well as those thereafter created.

Since the prudent man statute is essentially an investment rule, most of the law of trust administration and trustee's duties remains unaffected by its enactment. Moreover, many trusts gave trustees broad investment powers prior to enactment of the rule.

> instrument, a trustee is authorized to acquire every kind of property, real, personal or mixed, and every kind of investment, specifically including, but not by way of limitation, corporate obligations of every kind, and stocks, preferred or common, which men of prudence, discretion and intelligence acquire for their own account.

Since enactment of this section there have been no reported cases involving the propriety of an individual investment or diversification of a portfolio.[7] The prior legal list decisions are of little avail.[8] With the recent widespread adoption of the prudent man rule, including a modified version in New York, trustees in many other states face a similar interpretation problem as sufficient time has not elapsed for precedents to develop.[9]

California may draw upon the concepts and precedents of the principal source of prudent man law, Massachusetts. A reading of the Massachusetts decisions suggests that where a trustee acts in good faith within his authority and makes every effort to exercise the discretion of a reasonably prudent man, the courts, judging the act in light of the circumstances at the time of investment, are not likely to substitute their judgment.[10] The rule

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[7] Since there has been economic prosperity continually since 1943 and most investments have been successful, it may be too early for such cases which usually arise during financial depression.

In spite of the lack of reported decisions, the prudent man rule has been in active operation both in the probate courts and in guiding trustees' investments. However, the legality of a trust investment is not adjudged unless a demand for an accounting is made by a beneficiary except where the trustee petitions the court for approval or a corporate trustee files an annual account. Very few petitions for instructions are filed except where there is some question about the restrictions of a particular trust.

[8] In list states the permissible investments are expressly set out in statute or by court decision and none others are permitted unless the instrument so provides. Prudence is required even under the legal list, but the very nature of the list system obviates its present applicability. It is of interest to note, however, that in Day v. First Trust and Savings Bank of Pasadena, 47 C.A.2d 470, 118 P.2d 51 (1941), decided prior to the enactment of the prudent man rule, the court proceeds entirely as a prudent man court citing many usual Massachusetts rules. Considering the date of this case, it is questionable whether this dicta is embedded in California prudent man law.

[9] Six states have become prudent man jurisdictions in the last three years, swelling the total to twenty-four by case or statute. Most of these jurisdictions have enacted the rule within the last ten years. BOGERT, TRUSTS AND TRUSTEES, §§ 616-663 (1935) (pocket supp. 1950).

Long the most staunch advocate of the legal list system, New York modified its statute in 1950 to provide expressly that non-legals (listed common stock included) may be purchased up to 35% of the aggregate market value of the fund, thus supporting the suitability of common stock, diversification and the prudent man rule for trustees' investment. *Id.* at § 645 (pock. supp. 1950). This is but one phase in the growing shift of legal list jurisdictions to the more flexible prudent man rule. See Shattuck, *Important Development in Field of Fiduciary Administration,* 24 B. U. L. REV. 80 (1944).

New York law does not limit the effect of any trust which has specifically defined investment powers and it has been estimated that two-thirds to three-fourths of the trust funds in New York are unrestricted as to investments, Sayre, *Prudent Man Rule for Trust Investments,* 89 TRUSTS AND ESTATES 706 (1950). It is reported that the primary reason for the New York change was income considerations, Torrance, *New Trust Investment Law,* 89 TRUSTS AND ESTATES 300 (1950).

[10] *E.g.,* Kimball v. Whitney, 233 Mass. 321, 123 N.E. 665 (1919) (excellent elaboration of the rule); Taft v. Smith, 186 Mass. 31, 70 N.E. 1031 (1904); Bowker v. Pierce, 130 Mass. 262 (1881); Harvard College v. Amory, *supra* note 6. See Shattuck, *The Massachusetts Prudent Man in Trust Investment,* 25 B. U. L. REV. 307 (1945), intended for use in jurisdictions with newly enacted prudent man statutes for information on the Massachusetts decisions and applications; the rule is annotated phrase by phrase. See, also, RESTATEMENT, TRUSTS, MASS. ANNOT.

is admirably flexible and its only rigidity is that "faithfulness is prescribed and speculation prohibited."[11] Under the prudent man rule the responsibility is on the trustee, not the legislature. He requires more investment proficiency than trustees in legal list states and is never quite certain of his prudence or liability. Yet, "surcharges arise most often out of situations which involve a 'mosaic of negligence or default', breaches of loyalty and other deficiencies in combination. A surcharge is almost never founded upon the single ground that a trustee purchased an unpermitted security."[12] Disloyal dealings, however, are always grounds for surcharge.[13] Inevitably, there is no explicit guide for the trustee; he must merely use the "judgment of men of prudence, discretion and intelligence."[14]

Until a proper case is decided, California trustees will not know how the California rule may be interpreted, as for example, what dispositions are "prudent".[15] Conservative trustees may be limiting the risk, and hence income, of their funds apprehensive of the application of the rule. Such an approach belies a true understanding of the prudent man theory. The investments of a fiduciary are not judged by hindsight, but must be prudent as of the time made.[16] Subsequent declines in value will not bring surcharge unless accompanied by negligence.[17] No two trust situations can be alike, even though corpus, beneficiaries and instrument are similar, because economic and financial currents are constantly changing. There can be no

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[11] Shattuck, *supra* note 10, at 315.

[12] Shattuck, *supra* note 10, at 311. See Moore, *A Rationalization of Trust Surcharge Cases*, 96 U. OF PA. L. REV. 647 (1948).

The Massachusetts court has deemed itself obligated in the social interest to maintain a kindly and understanding attitude toward trustees, Shattuck, *supra* note 314. "Trustees are justly and uniformly considered favorably . . . provided they conduct themselves honestly and discreetly and carefully according to the existing circumstance." Putnam, J. in Harvard College v. Amory, *supra* note 6.

[13] SCOTT, TRUSTS § 170 (1939); *cf.* CAL. CIV. CODE §§ 2228, 2229, 2230, 2231, 2232.

[14] Evidence of prudence includes expert testimony by other trustees and evidence of the nature and extent of investigations made by the trustee. Memoranda showing recognition of the various attendant factors at the time should minimize surcharge, and form an adequate basis for the exercise of discretion. See SCOTT, TRUSTS, *supra* note 13, § 227.

[15] There is wide divergence as to what constitutes prudence, SCOTT, TRUSTS, *supra* note 13, § 227.5. This divergence is primarily due to the existence of the two basic rules, New York's list and Massachusetts's prudent man. "It is doubtful whether the rules are distinct in theory but the fact remains that in operation they have produced sharply conflicting results." Shattuck, *supra* note 10, at 309.

SCOTT, TRUSTS, *supra*, § 227 repeats the language of *In re* Est. of Cook, 20 Del. Chan. 123, 126, 171 Atl. 730, 731 (1934), with approval: "A trustee must use the caution in making investments which is used by prudent men, who have primarily in view the preservation of their property, who are *safeguarding the property for others*." (Emphasis added.) Many courts make such a distinction from the traditional approach: " . . . in the management of their own affairs." Should it matter whether the trustee in observing the requirements of prudence does so in regard to his own affairs or those of others so long as he observes them? The fact remains that many trustees do not acquire certain investments for the trust portfolio that as prudent men they would buy for their personal account. This moral compunction and conservatism may not allow the prudent man standard to realize its intended purpose.

[16] First National Bank of Boston v. Truesdale Hospital, 288 Mass. 35, 192 N.E. 150 (1934); Green v. Crapo, 181 Mass. 55, 62 N.E. 956 (1902); Taft v. Smith, *supra* note 10; Bowker v. Pierce, *supra* note 10; Costello v. Costello, 209 N.Y. 252, 103 N.E. 148 (1913). CAL. CIV. CODE § 2261 provides: ". . . under the circumstances then prevailing . . . ."

[17] *Ibid.*

precedents or stare decisis as to what particular investments are prudent. An investment in one case that is improper may be proper at a different time or in a different trust because of changed circumstances.[18] For a proper application of the rule the California courts should treat each case separately on its own facts; otherwise, a court-made "legal list" will develop.

It would serve no useful purpose, if the true concept of the rule is that each case is unique, to review all the decisions of Massachusetts as to the propriety of an investment. Even real estate, junior mortgages, unsecured obligations and participating mortgages are not necessarily prohibited in Massachusetts,[19] although investments in trade or business are.[20] There has never been any doubt as to common and preferred stocks where choice of the amount and the company is prudent, and now the statute expressly permits such investment.[21] In justification of the rule it is said that no specific kind of investment, even if in the form of fixed income indebtedness, can ever be said to be absolutely safe. "Do what you will, the capital is at hazard."[22]

The rule does expressly prohibit speculation. Most prudent men should be able to agree at a given time what would be speculation. It would probably include margin purchases, selling short, "trading" on temporary changes in market price, and buying securities of new and untried companies or those inherently risky or defective in security and marketability.[23]

Because of the dynamic nature and inherent risk in equity securities as well as the old adage concerning eggs and a basket, the Massachusetts courts have usually seen fit to impose a duty of diversification, regardless of the excellence of the security.[24] In other words, it is usually "prudent" to diversify. Diversification arises in two senses: (1) division of the fund between equity securities and fixed income-debt securities (diversification as to type of security) and (2) avoidance of investment of a substantial portion in any one company, regardless of type of security (diversification

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18 Massachusetts does not seem to permit a decision in one case to be a precedent for another. *E.g.*, Taft v. Smith, *supra* note 10, and Dickinson Appellant, 152 Mass. 184, 25 N.E. 99 (1890).

19 Shattuck, *supra* note 10, at 321.

20 Digney v. Blanchard, 226 Mass. 335, 115 N.E. 424 (1917); Warren v. Pazolt, 203 Mass. 328, 89 N.E. 381 (1909); Trull v. Trull, 13 Allen 407 (Mass. 1866).

21 *E.g.*, *In re* Buhl's Estate, 211 Mich. 124, 178 N.W. 651 (1920); Note, 12 A.L.R. 574 (1921); BOGERT, *op. cit. supra* note 9, § 679; SCOTT, TRUSTS, *supra* note 13, § 227.11.

22 Putnam, J. in Harvard College v. Amory, *supra* note 6.

23 LORING, A TRUSTEE'S HANDBOOK 156 (Shattuck ed. 1940). BOGERT, *op. cit. supra* note 9, § 612.

24 Warren v. Pazolt, *supra* note 20; Davis Appellant, 183 Mass. 499, 67 N.E. 604 (1903); see Dickinson Appellant, *supra* note 18; RESTATEMENT, TRUSTS § 228 (1935); SCOTT, TRUSTS, *supra* note 13, § 228; 54 AM. JUR. §§ 380, 417. Diversification was not required in First National Bank of Boston v. Truesdale Hospital, *supra* note 16. Many jurisdictions (the legal list states) do not impose a duty of diversification, *e.g.*, *In re Beebe's* Estate, ... Misc. ...., 52 N.Y.S. 2d 736 (1943), *aff'd*, mem., 268 App. Div. 1051, 52 N.Y.S. 2d 796 (1945); SCOTT, *supra* note 13, § 228; Note, 131 A.L.R. 1158 (1941).

There is no liability for failure to diversify where the loss would have occurred anyway, NOSSAMAN, TRUST ADMINISTRATION AND TAXATION § 464 (1945).

The Massachusetts courts have not fully discussed diversification as to maturities and location, SHATTUCK, *supra* note 10, at 324.

as to business identity). Older cases, such as *Dickinson Appellant*,[25] state that the investment of 50% of the fund in common stock would be an ultimate limit, while *Davis Appellant*[26] surcharged a trustee for holding more than one-third of the fund in securities of one company. However, any impression that courts would set up definite percentages would seem to have been corrected in a later decision by the Massachusetts court which clearly asserted that no arbitrary rule has ever been adopted in that state.[27] It is hoped that such an interpretation will be followed in California. How much of the fund may be invested in common stock or the securities of a particular corporation is thus discretionary; the important question is what proportion, under the circumstances, is prudent.[28] Various considerations regarding the prudence of a particular stock have been mentioned by the courts, but these in sum amount to very basic considerations commonly applied to investments.[29]

In practice, the California courts seem to avoid becoming investment advisors and rarely make an independent judgment as to the prudence of a particular investment disposition. The courts refuse to recommend investments and, giving great deference to the professional acumen of trustees, approve any investment submitted unless its unsuitability is beyond question. However, the courts do seem to urge diversification.

Investment Duties to the Income Beneficiary

Under the classic statement of the prudent man rule, the trustee has a twofold duty to consider "*the probable income as well as the probable safety of capital.*"[30] The California statute similarly embodies this principle. Some courts and writers, however, perhaps motivated by undue solicitude for the remainderman, have distorted the coequal duty to provide income and have espoused the rule that the primary duty is safety of prin-

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25 *Supra* note 18.

26 *Supra* note 24.

27 North Adams National Bank v. Curtiss, 278 Mass. 471, 180 N.E. 217 (1932) (by dictum only, but deliberate). And see New England Trust Co. v. Paine, 317 Mass. 542, 59 N.E.2d 263 (1945), where the court said there was no hard and fast rule on the extent of diversification required.

28 See notes 58-63 *infra*. Boston trustees have followed the practice for some time of balancing the portfolio 50% in common stock, SHATTUCK, *supra* note 10, at 323. Many courts, including some in California, have approved amounts up to 100% in small trusts where income was essential. *In re* Rees Estate, ...Ohio App......., 85 N.E.2d 563 (1949), did not surcharge a trustee although 71% of the fund was invested in common stock, when there were factors supporting liberality.

29 *E.g.*, "Trustees . . . are permitted to invest . . . in dividend paying stocks . . . when the corporations have acquired by reason of their property and the prudent management of their affairs such a reputation that cautious and intelligent persons commonly invest their own money . . .", Dickinson Appellant, *supra* note 18. Similarly, *In re* Buhl's Estate, *supra* note 21, the tests were that the corporation had been in business a considerable time, its record of earnings was good and there was no reason to anticipate a diminution of earnings. Railroad stocks were permitted where the corporation had a long history of productive returns, was located in a prime industrial area, was conservatively capitalized, was readily marketable and had future income capacity assured. New England Trust Company v. Paine, *supra* note 27.

30 Harvard College v. Amory, *supra* note 6; *accord*, Taft v. Smith, *supra* note 10; Dickinson Appellant, *supra* note 18; Kinmonth v. Brigham, 5 Allen 270, 278 (Mass. 1862).

cipal, and productivity is secondary.[31] Yet, the trustee is under a positive duty to make the corpus productive and unless directed otherwise must maintain an impartiality to the interests of the life tenant and remainderman.[32] Therefore, any substantial deviation from treating these interests equally would be a departure from the required equable mean. In making investments it would not be heretic, especially in view of present economic effects on income beneficiaries, to give at least full thrust to the classic statement of the rule and fairly balance the necessity of income with safety.

The importance of income should rest, of course, on the testator's intentions and directions. But where the testator makes no provision for subsequently declining real income, the trustee must ask himself what the settlor would have preferred. Where the income cestui is the widow and the remainder is to grown children or to a charity, most testators would probably prefer maintenance of a satisfactory living standard to preservation of corpus; in fact it is now quite common for the trust instrument to provide for invasion of corpus for income in such situations.[33] Who the beneficiaries are and their particular needs and sources of income are material to whether income should be of more than coequal importance.[34] Since the income tenants are often members of the testator's immediate family, a strong argument can be made for the maintenance of a livable income regardless of a somewhat higher element of risk to principal. This does not mean, however, that any shifting of investment emphasis to productivity should be done outside the confines of the prudent man standard. To be sure, there will be little or no income if principal is impaired as a result of high risk investments. But the issue is merely one of placing emphasis on income where there is a choice among prudent investments.

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[31] *E.g., In re* Est. of Cook, *supra* note 15; Scott, Trusts, *supra* note 13, § 227; *In re* Buhl's Estate, *supra* note 21; Brown's Estate, 287 Pa. 499, 135 Atl. 112 (1926).

One might question the veneration given the safety of principal idea of preserving and passing on the same number of dollars when in fact they do not represent what they formerly did. Recoverability as a guide should at best be only a minimum standard and not a maximum if value is to be preserved. One writer in asking what does "safety of principal" mean suggests that although the traditional meaning is in recoverability or stability of original dollar investment, it should be interpreted in light of real values; more attention should be focused on the influence of purchasing power on safety of principal. He submits that the phrase safety of principal is illusory and might better be forgotten, thus causing the objectives to be spelled out more specifically. Hayes, *supra* note 5.

[32] Bogert, *op. cit. supra* note 9, §§ 611, 612; Restatement, Trusts §§ 181, 232 (1935); Scott, Trusts, *supra* note 13, § 232. The balancing of interests controls the amount of risk that will be undertaken in order to provide income higher than the prime interest rates. It is naturally difficult to say what diversification of investments properly puts in balance the interests of income and safety. It would seem that a trustee may invest a large portion of a fund in higher yielding equity securities before the interests could be said to be truly balanced. Trustees are, however, given great discretion in striking a balance.

[33] See note 90 *infra* for recent cases regarding invasion and deviation.

[34] Matter of Hess, 171 Misc. 690, 13 N.Y.S. 2d 701 (1939) cites a series of cases where the interpretation of the investment powers clause was dependent on the relationship of the beneficiary to the testator. "In other cases such intention [referring to the intention of the testator that the trustee should obtain the highest return consistent with safety of principal] is derived largely by inference from the fact that the beneficiaries were the widow and or the infant children."

See Stone, *Life Tenant v. Remainderman,* 84 Trusts and Estates 530 (1947), asserting that the life tenant is the primary object of the donor's affection. Relationship is also one of the strong factors in invasion or deviation cases.

Consideration of Purchasing Power in Trust Management

Should a trustee governed by the prudent man rule be under a duty to consider the purchasing power of the dollar in making investments?[35] The dollar income originally intended by testators may later become inadequate unless declines in purchasing power can be offset. Many trustees, aware of this, would admit that under usual, conservative investment policy the income tenant may during the present inflation be deprived of a previous normal living standard, but would argue that to offset declining purchasing power in the making of investments would be to increase risk along with income and thus prejudice the interests of the remaindermen. Such an approach overlooks both that there are investments which hedge against inflation without being detrimental to the remainder and that coequality of income is required, tempered by the presence of life tenants closely related to the testator.[36]

To impose an absolute duty to be guided by purchasing power in investing may be too harsh and rigid. Purchasing power may be relatively unimportant in certain trusts and in others the trustee may not have the facility to use anti-inflation investments or may find it impracticable. A far better approach is that of the prudent man philosophy—in a particular situation, would it be imprudent not to consider purchasing power? Despite expressions to the contrary, trustees should recognize that purchasing power and adequate income are important factors in prudent management.[37] Clearly, hardship to the income beneficiary may occur uuless where possible investments are made which yield increased income reasonably proportionate to increases in cost of living.

Of course, trustees can and should be held liable for failure to produce a reasonable income as a result of undue conservatism.[38] Thus the ultra conservative trustee may conceivably be held liable for unnecessarily favoring the remainder and not producing an income comparable to other trust yields, where there is no adequate justification for his policy.[39] One recent case took a similar outlook and the trustee was held under a duty to provide a higher income than that obtainable solely from government bonds.[40]

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[35] In legal list states where the trust instrument does not give liberal investment powers, the trustee has no alternative except to follow the list composed ordinarily of fixed income obligations vulnerable to inflation.

[36] Common stocks are the outstanding example. Slightly increased risk (decline in market value, due to market oscillations) is more than offset by the ability to steadily increase in value with changes in price level.

[37] *E.g.*, Headley, *A Trustee in a World of Changing Values*, 5 LAW AND CONTEMP. PROB. 355, 365 (1938).

[38] SCOTT, TRUSTS, *supra* note 13, § 232. A trustee is under a duty not to purchase property which yields an income substantially lower than that which is normally earned by trust investments.

[39] *Ibid.*

[40] In Security Trust Co. v. Mahoney, 307 Ky. 661, 212 S.W. 2d 115 (1948), the entire trust fund was invested in 2½% U. S. bonds and the income was inadequate for support of the life cestui; the court held it to be the duty of the trustee to invest a reasonable part of the capital in conservative investments bringing a higher income since the trustee is under a duty to seek reasonable income as well as safety and to deal impartially in securing these objectives. The prudent man court authorized common stock up to 75% of the fund.

At least part of the beneficiary's battle with inflation thus may be won through a cognizant judiciary.

Common Stock as a Prudent Trust Investment

It is one thesis of this comment that the most important and desirable interpretation which can be given to California's prudent man statute is one which does not penalize or discourage the purchase of fairly high proportions of sound common stock for protection against inflation and production of satisfactory income.

Even though the common stock of many corporations is a prudent investment, some attorney-trustees have not favored its use.[41] As an inflation hedge, common stock values—both market and underlying book values—have kept pace with the rising price level much better than other investments, thus benefiting the remainder.[42] More important than this increase in value, since appreciation is not usually helpful to the income beneficiary,[43] is the maintenance of a high, regular and often increasing income

[41] An unpublished survey of 420 attorney-fiduciaries in November, 1949, by Scudder, Stevens and Clark (investment bankers) indicated 15% do not, in general, favor the use of common stock for trust investment where the law permits it.

[42] Where timing of purchases has been satisfactory, equity prices and earnings have increased reasonably in proportion to the rising price level. One eminent economist has appraised the rise in net worth of all American manufacturing corporations in the decade 1940-50 at 111%, while market value of all stocks listed on the New York Stock Exchange was increasing 64% in the like period. Jacoby, *Personal Investment Policy*, 89 TRUSTS AND ESTATES 770, 772 (1950):

The Wholesale Commodity Price Index (B. L. S.) rose 138% from average 1939 level to February, 1951; Standard & Poor's Common Stock Price Index rose 75% during the same period. (See note 1 *supra* for data indicating a rise in a similar period of 78% in the Consumers Price Index.)

Dividends paid by 82 corporations with individual assets over 50 million dollars (including dividends on preferred stock) increased over the 1939 amount: 52½% in 1947, 84½% in 1948, 125% in 1949 and in 1950, 207%. 37 FED. RES. BULL. 425 (1951). According to one statistical series by the Federal Reserve Bulletin (discontinued after 1948) dividends on common stock for 152 corporations increased 49% from 1939 in 1947, and 81% in 1948. 35 FED. RES. BULL. 552 (1949).

Obviously, fixed income securities are vulnerable to inflation through depreciation in value of the fixed number of dollars they regularly earn and those repaid at maturity. Purchasing power risk is inevitable to some degree in any investment in a dynamic economy, but depreciation in the value of the unit (purchasing power) can be offset by more units (dollars), *i.e.*, higher income and increasing market value. Common stocks satisfy this necessity, by giving more dollars of income to the life tenant and increasing value to the remainderman. While there does not seem to be any direct relation of earnings and stock prices to general price levels, yet, generally, rising prices increase business profits and stock market prices.

Smith first demonstrated in 1924 that the safety of bond investment was largely illusory when allowance is made for loss of purchasing power and the possibility of severe cyclical adversity, SMITH, COMMON STOCKS AS LONG TERM INVESTMENT 92-100 (1924). See BADGER AND GUTHMANN, INVESTMENT PRINCIPLES AND PRACTICES 252-63, 69, 70 (2d ed. 1942) for an amplified comparison of common stocks and bonds as long term investments.

Equity securities are a better hedge against inflation than the other usual anti-inflation alternatives, international currencies or securities, gold, commodities and real estate, each of which is subject to substantial disadvantages or impossibilities as trust investments.

[43] Appreciation, one of the principal objectives in long term common stock investment, does not work favorably for the income tenant where the Uniform Principal and Income Act applies (in California, 3 GEN. LAWS, Act 8696 (Deering 1944)), since profits resulting from changes in principal inure to the principal, § 3. This result can be avoided in drafting, see note 8, *infra*. Similarly, the very favorable capital gains tax on such transactions, while an important incentive to investment in common stock for appreciation, does not benefit the income tenant.

yield.[44] The prosperity that has spurred inflation has provided unusual sales and profits.

Present day purchases of common stock will not, however, be apt to offset further inflation in living costs unless profits and dividends accordingly increase. There are factors present that may prevent this.[45] Yet if, as expected by most economists, the inflation and prosperity era continues, most corporate results will be favorable. Many dividend rates are protected by substantial present earning power and future earning capacity; many companies have been conservative in declaring a low percentage of earnings as dividends in order to maintain a steady return; hence, a decline in earnings may not affect the maintenance of present dividend rates. Perhaps the strongest argument for common stock is not as a perfect inflation hedge, but that, comparative to risk, in an era where substantial income is required, yields are and should remain adequate, whereas those from bonds are not.[46]

These arguments for common stock are based on the underlying fact that the issues of many companies have achieved investment status.[47] Primarily, these are large, well managed concerns, able to maintain satisfactory stable markets without serious competitive risks, often producers of consumption goods. There is ample statistical evidence to demonstrate the maintenance of a satisfactory stable return on many equity securities over long periods of time including depression.[48] As the economy continues its

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[44] See note 42 *supra* for trend of dividend payments. Yields have been maintained from 1947 to date in the better companies at 5-7% in spite of reduced dividend payments due to increased retention of earnings for expansion purposes. See note 48 *infra*. The great surge in security prices since late 1949 has served to lower yields, yet with expansion substantially ended, higher profits and dividend pay-outs have kept yields near 6%. 12 THE EXCHANGE 1 (January 1951). Yield on cost of many securities purchased between 1939-1942, if held today, would show increases of over 100%, which more than compensates for the increased costs of living during the past ten years. *E.g.*, 1940 yield at average 1940 market price was 7.6% for Chrysler, 5.85% for Swift & Co., 5.0% for Texas Co.; 1950 yield on same market price was 27% for Chrysler (adjusted for split up), 11.5% for Swift & Co., and 17.9% for Texas Co. (MOODY'S INVESTOR'S SERVICE 1940, 1950.) Prewar yields were in the 4-5½ area generally.

[45] Inflation increases business costs, causing profit margins to be squeezed. Some of this increase has been passed on in sales price, and substantial volume has kept profits high, but with high and rigid breakeven points, profits are very sensitive to slight changes in volume. Higher taxes, controlled prices, alloeation of materials, and regulation of output seriously threaten the maintenance of present profits in many companies.

[46] The decline in bond yields to below 3% leaves them lagging common stock yields by 3 to 4%; bond yields may be expected to continue at these low levels with only moderate improvements presently in evidence. See note 2 *supra* for bond yield data and see notes 44 *supra* and 48 *infra* as to stock yields.

[47] Generally defined as ability to earn an adequate return and pay dividends over long periods of time without interruption or great variation in amount and a lack of great fluctuation in market price except in response to general market and business trends.

[48] In 1948 and 1950, 89% of all stocks listed on the New York Stock Exchange paid dividends which yielded an average 7.8% in 1948 and 6.7% in 1950.

Approximately 30% of all listed stocks have paid consecutive dividends at least twenty years; the average yield on these securities as of the end of 1950 was 6.1%; over half the listed securities have paid dividends consecutively for ten years. Fifty-seven companies (5%) have paid dividends over fifty consecutive years. Roughly only 10% of the listed companies are not presently paying continuous dividends. Even though these yields are averages, containing some high risk-yield companies, there are many "blue chip" securities ineluded in the 5-7% bracket secular growth, well managed companies will be able to share in the continuing demand. However, success of common stock as an investment medium is not general, but confined to selected industries and companies.

Equity prices generally fluctuate widely within periods as short as a few months to two or three years.[49] But common stock as an investment should be held and not traded actively as a speculator might do. Common shares should be regarded as the least liquid item in the portfolio to avoid losses from sales at depressed market prices. Sales should be only for the purpose of improving the investment position or realizing appreciation. Therefore, market price fluctuations are not an important risk except when liquidation may become necessary.[50] Of course, common shares, and to a lesser extent preferred shares, being residual ownership interests, bear the major brunt of all business risk: governmental influences, technological changes, decline or shift in demand and cyclical depression. Quality issues are able to adjust reasonably well to such risks, or are impervious.

One disadvantage of common shares is the ability and time necessary for proper management. Successful common stock investment requires fairly constant vigilance, review, analysis and ability to make proper judgments regarding selection of issues and timing of transactions. This subjective element is a prime determinant of how much stock a non-corporate trustee is willing to undertake, as the success or failure of investment in equity securities depends ultimately on selection and timing.

Not all common stocks are of investment quality; in fact, only a small proportion can qualify. The emphasis in common stock investment should be on value rather than on financial strength.[51] If the valuation is accurate, the principal should be "safe" regardless of market fluctuations.[52] Valuation, however, is based primarily on estimates of earnings which are subject to some degree of error.[53]

There are at least three approaches to common stock investment: (1) selecting only the "blue chips"; (2) selecting growth issues; (3) selecting undervalued issues.[54] The blue chips often stress stability of income and price to the exclusion of value to such a point that relative to risk they are

(although dividends may be consecutive, they may vary in amount from year to year), REPORT, NEW YORK STOCK EXCHANGE (1950). See MERRILL LYNCH, PIERCE, FENNER AND BEANE, DIVIDENDS—YEAR AFTER YEAR (1951).

[49] These short term oscillations have often obscured the fact that equity prices show a continuing long term appreciation. See chart, BADGER AND GUTHMANN, *op. cit. supra* note 42, at 251.

[50] Assuming liquidity is not essential and valuation is intelligent, the safety of principal of funds in common stock is not impaired by market fluctuations, GRAHAM, THE INTELLIGENT INVESTOR (1949).

[51] DOWRIE AND FULLER, INVESTMENTS 498-519 (2d ed. 1950).

[52] Hayes, *supra* note 5, at 389.

[53] The most important indication of value is the price earnings ratio, wherein the earnings factor is commonly based on an average of past earnings experience. However, past earnings are not necessarily a guide to future value, and attempts to use estimated future earnings in the ratio may fail due to the uncertainties of estimation, see Hayes, *supra* note 5, at 391; DOWRIE, *op. cit. supra* note 51, at 512-15. Traditionally the accepted ratio for better stocks has been 12-15.

[54] DOWRIE, *op. cit. supra* note 51, at 501. *Cf.* GRAHAM & DODD, SECURITY ANALYSIS 351-371 (2d ed. 1940).

overpriced and thus yield too little compared to other good securities; yet, they are useful to the busy or inexperienced investor. Growth stocks are expected to appreciate in both income and principal but may also be overpriced; moreover, the problem of selecting the right industry and company is present. Purchasing undervalued, sound issues is generally the most successful method of common stock investment. Undervaluation occurs occasionally due to psychologically depressed markets and absence of current information or analysis.

Common stock cannot be recommended absolutely,[55] but in most circumstances a trustee can reasonably invest a sizeable portion of a fund in common stock as a prudent investment, providing adequate care is taken in selection and supervision.

How much Common Stock is Prudent?

The balanced fund, composed of fixed income securities and equity securities, has shown the best results, is theoretically the best approach to long term investment, is most widely advocated and may be mandatory if diversification is required.[56] Assuming a normal trust situation, how much of a fund properly should be invested in common stock? It is difficult to generalize, as the circumstances of each trust are dissimilar, but as an aid or guide the proportions placed in common stock by other investment funds may be examined.[57] The endowment funds of five of the largest private universities were invested at the end of 1950 from 43.0% to 50.7% in equity securities and the total funds were yielding in excess of 4.0%; it was reported that these funds would buy or sell with market price changes to maintain these percentages.[58] A recent survey of all common trust funds in existence more than one year indicated an average of 38.8% of each fund held in common stock.[59] Trust accounts of bank fiduciaries are now averaging 40 to 50% in common shares.[60] Boston trustees have long held roughly one-half of their trust funds in equity securities.[61] Investment trust companies show a wide range in percentage holdings of common stock but most are holding considerably more than 40 to 50%.[62] Many fire insurance companies have a substantial proportion of their portfolio in equity securities.[63]

[55] At very high price levels, yields are so reduced that comparative to risk, equity shares lose much of their attractiveness. The nearness of large liquidation or importance of tax or safety considerations also reduce their utility.

[56] DOWRIE, *op. cit. supra* note 51, at 105, 135; CARPENTER, INVESTMENT TIMING BY FORMULA PLANS (1943). The proportions of debt and equity securities may be varied from time to time with changes in the stock market or economic conditions. There are many variations of predetermined automatic shifting plans known as formula plans, see Carpenter, *ibid.*

[57] There is, however, no judicial determination that these proportions are prudent within the meaning of the prudent man rule for trust investments.

[58] Wall Street Journal, Jan. 29, 1951, p. 11, col. 2.

[59] 89 TRUSTS AND ESTATES 741 (1950).

[60] Discussion with bankers well acquainted with general practices as well as informal surveys conducted by the trust section of California division of American Bankers Association confirms this conclusion. See 88 TRUSTS & ESTATES 156 for amounts held in 1949.

[61] *Supra* note 28.

[62] DOWRIE, *op. cit. supra* note 51, at 254-6; WIESENBERGER, INVESTMENT COMPANIES (1950).

[63] DOWRIE, *op. cit. supra* note 51, at 238; SPECTATOR INSURANCE YEARBOOK (FIRE AND MARINE) (1949).

Admittedly, these large funds have expert staffs for selection and timing, but the very fact of their expertness lends weight to the conclusion that 40 to 50% is not an imprudent proportion when skill and vigilance is available, but one that should be achieved in order to provide adequate income.

In the final analysis, within the limits of the prudent man rule, the necessity for liquidity and income, plus the managerial capacity of the trustee, will determine the extent common stock should be employed. It is likely that there are trustees who are holding less than one-third of the fund in equity securities. Where justified by special circumstances, there can be no objection; but, where a trustee is holding such a low proportion in common stock he may be depriving the income cestui of needed income. Clearly, prudent men would buy a larger proportion of common stock under present circumstances.[64]

Alternative Anti-Inflation Security Investments

Some writers have advocated the use of investment trust shares not only as reasonably good income producers but also because they solve the problems of selection, management, timing and diversification for the trustee.[65] The law seems unsettled whether this type of investment will be permitted, the principal objection being one of undue delegation. Contrasted to other permissible investments, this does not seem a valid objection since the same amount of delegation exists in bank and insurance stocks or, in fact, common stocks in general. At least one progressive court has allowed its use.[66] These shares have not, however, received widespread acceptance among trustees, objection being made to the high loading charge (acquisition cost) and management fees.[67] But, for the trustee without sufficient time and ability, this type of investment would definitely be of great assistance and would seem to qualify under the prudent man rule.

Preferred stocks, while fixed income type securities, offer some attraction because they provide higher yield than bonds.[68] Most investment portfolios contain some preferred shares, and those with participating or conversion privileges may be especially attractive. However, many believe that preferred shares have none of the advantages of common shares, all of the disadvantages of bonds and an ownership risk for which the yield does not

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[64] It is not contended that the many factors which make high proportions of common stock prudent under present conditions will require similar proportions in changed economic circumstances. But many common stocks can be successfully held as long term investments irrespective of changing economic conditions including cyclical depression.

[65] Shattuck, *Propriety of Investments in Investment Trusts,* 25 B. U. L. Rev. 1 (1945); Stevenson, *Investment Company Shares,* 89 Trusts & Estates 228 (1950). See, also, a previous series of articles by same author in 84–85 Trusts & Estates, later published in book form; Dillin, *May Trustees Invest in Investment Trusts,* 89 Trusts & Estates 396 (1950).

[66] *In re* Rees Estate, *supra* note 28, 34 Minn. L. Rev. 163.

[67] Results of a survey of 801 lawyers and trust officers in November, 1949 conducted by Scudder, Stevens & Clark Co. disclosed only 10% purchase such shares for small trusts.

A questionnaire sent to California fiduciaries by the California Bankers' Association in 1947 indicated only one in twenty were using investment trust shares, 85 Trusts & Estates 430 (1947).

[68] *E.g.,* in May, 1949, high grade preferreds were averaging 4.0% yield; in August, 1950, approximately 3.75%. *Cf.* note 2 *supra.*

adequately compensate; the fixed regularity of dividends is often illusory.[69]

In addition to investment practices there are certain other procedures which may be used to obtain an adequate support for the income tenant during inflation. More satisfactory than devices used only after hardship has arisen are those which make possible the necessary protection through preventive or enabling measures.

Drafting the Investment Clause

The settlor may direct the manner in which the fund shall be invested, and his directions bind the trustee.[70] He may express his intent that provision of a satisfactory income for the life tenant is more important than preservation of principal. A trustee may be restricted to a class of investments narrower than would be permitted in Massachusetts, or may be authorized to make investments that would not be permitted.[71] The latter direction would not likely be provident in a prudent man jurisdiction; the prudent man rule is as flexible and liberal as needed. The presence of such words as "in his discretion" has not liberated the trustee from the operation of the rule.[72] However, liberal investment powers can do a maximum of good in legal list states.[73]

Exoneration or exculpatory clauses allow trustees in prudent man states the widest investment powers with liability only for willful default or bad faith, thus suspending, to a certain extent, the restrictions of the rule.[74] But where is the line to be drawn between imprudence and willful default?[75] Exoneration clauses may serve to reduce undue conservatism in fear of surcharge, but other serious policy disadvantages must consciously be weighed with this advantage.

A more common method of insuring adequate income to the tenant is to permit invasion of principal when in the trustee's discretion this is neces-

69 *E.g.*, GRAHAM & DODD, *op. cit. supra* note 54, at 186-190, 194, 195; Niebling, *Now Nobody Wants Preferred Stocks*, BARRON'S 25 (Mar. 29, 1948); Thomas, *Are Preferred Stocks Conservative?*, 90 TRUSTS & ESTATES 152 (1951). The shareholders' rights in the preferred share contract have already been shown to be of little value due to the ease of alteration by amendment or merger. See McNulty v. W. & J. Sloane, 184 Misc. 835, 54 N.Y.S. 2d 253 (1945); Sherman v. Pepin Pickling Co., ...Minn........, 41 N.W. 2d 571 (1950); Federal United Corp. v. Havender, 24 Del. Ch. 318, 11 A.2d 331 (1940); Langfelder v. Universal Laboratories Inc., 163 F. 2d 208 (3d Cir. 1947).

70 SCOTT, TRUSTS, *supra* note 13, § 227.14; CAL. CIV. CODE § 2258; BOGERT, *op. cit. supra* note 9, § 681; Stephenson, *Trust Investment Provisions Which have Worked Well*, 5 LAW. & CONTEMP. PROB. 377 (1938); Comment, 58 YALE L. J. 288 (1949).

71 SCOTT, TRUSTS, *supra* note 13, § 227.14; Comment, 58 YALE L. J. 288 (1949).

72 Davis Appellant, *supra* note 24; Brown v. French, 125 Mass. 410 (1878).

73 SCOTT, TRUSTS, *supra* note 13, § 227.14; Comment, 58 YALE L. J. 288 (1949). In legal list states, if the instrument confers broad discretionary powers to invest in non-legals the trustee may do so if with due care; the powers thus are similar to the Massachusetts rule. Guaranty Trust Co. v. Fisk, 244 App. Div. 200, 278 N.Y.S. 809 (1935), *aff'd mem.*, 270 N.Y. 550, 200 N.E. 312 (1936); Fox v. Harris, 141 Md. 495, 119 Atl. 256 (1922); *In re* Hall, 164 N.Y. 196, 58 N.E. 11 (1900).

74 Such clauses are generally held valid, New England Trust Co. v. Paine, *supra* note 27; RESTATEMENT, TRUSTS § 222; Note, 158 A.L.R. 262 (1945); Shinn, *Exoneration Clauses in Trust Instruments*, 42 YALE L. J. 359 (1933). There is no prohibition in California, RESTATEMENT, TRUSTS, CAL. ANNOT. § 222 (1940).

75 See New England Trust Co. v. Paine, *supra* note 27.

sary for adequate care and support.[76] It is far better to reduce principal in sustaining income than to risk it all on doubtful high income securities during a period of economic instability.

Giving the trustee discretionary power to allocate receipts, gain in corpus, and expense between income and principal, thus displacing the operation of the Principal and Income Act,[77] can also enhance the income tenant's position.[78] The intent of the trustor to prefer the income beneficiary should be express in order to shape the trustee's discretion, since discretion does not necessarily insure an apportionment favorable to the income tenant. Therefore, the settlor may be well advised to direct the specific methods of apportionment favoring the income beneficiary.

Some thought might be given to the inclusion of power to distribute in kind in order to prevent the necessity of liquidation in adverse or depressed markets merely for distribution, where common stock is to be employed.

Consent

Even though liberal investment powers are not present to insure adequate income, it is well settled that where *all* beneficiaries consent to a breach of trust or unpermitted investment, they are estopped from surcharging the trustee.[79] Thus, a trustee by obtaining a release or consent may evade restrictive investment provisions (or possibly even the restrictions of the prudent man rule) and utilize more productive dispositions. In a low purchasing power era, the income beneficiary's consent would be forthcoming, but remaindermen are not estopped by the tenant's consent.[80] Furthermore, there are limitations on the doctrine of estoppel through consent.[81]

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[76] See NOSSAMAN, TRUST ADMINISTRATION & TAXATION § 276 (1945); Estate of Ferrall, 92 Cal. App. 2d 712, 207 P. 2d 1077 (1949); Whitaker v. McDowell, 82 Conn. 195, 72 Atl. 938 (1909); Burgin v. Patch, 312 Mass. 219, 44 N.E. 2d 684 (1942); *In re* Ohlson's Will, 208 Wis. 492, 243 N.W. 214 (1932). The court will not disturb such discretion if exercised in good faith, Wright v. Blinn, 225 Mass. 146, 114 N.E. 79 (1916).

[77] 3 CAL. GEN. LAWS, Act 8696 (Deering 1944).

[78] Section 2 provides that the settlor "may himself direct the manner of ascertainment of income and principal and the apportionment of receipts and expenses or grant discretion to the trustee . . . and such provision and direction . . . shall control notwithstanding this Act. The exercise by the trustee . . . of such discretionary power if in good faith . . . shall be conclusive . . . ." Thus, for example, if so provided, gains in principal from appreciation would not be required to be allocated to principal as § 3 would require.

[79] *E.g.*, RESTATEMENT, TRUSTS § 216; SCOTT, TRUSTS, *supra* note 13, § 216.

[80] BOGERT, *op. cit. supra* note 9, § 689; SCOTT, TRUSTS, *supra note* 13, § 216.2; White v. Sherman, 168 Ill. 589, 605, 48 N.E. 128, 132 (1897); Bennett v. Pierce, 188 Mass. 186, 74 N.E. 360 (1905); St. Germain v. Tuttle, 114 Vt. 263, 44 A.2d 137 (1945); RESTATEMENT, TRUSTS, CAL. ANNOT. § 216 (1940); Note, 128 A.L.R. 4.

[81] CAL. CIV. CODE § 2230; SCOTT, TRUSTS, *supra* note 13, § 216.3; RESTATEMENT, TRUSTS § 216.3: Consent does not preclude holding the trustee liable if: (a) the beneficiary is under incapacity at the time of consent, (b) the beneficiary, when he gave consent, did not know his rights and the material facts which the trustee knew or should have known, (c) the consent was induced by improper conduct of the trustee, (d) the beneficiary was not of competent age or understanding, and (e) the trustee had an adverse interest and the transaction was not fair and reasonable.

Estate of Van Deusen, 30 Cal.2d 285, 182 P.2d 565 (1947), asserted that the consent must be of *all* beneficiaries; however, it does not appear fully settled in this jurisdiction if this includes unborn beneficiaries. *Cf. In re* Boyles Estate, 252 Wis. 511, 32 N.W.2d 333

Deviation and Invasion

Where there is no provision for an advance or invasion, or there are restrictions on investments which prevent the earning of adequate income, courts may nonetheless allow the trustee, upon appropriate petition and showing, to deviate from the terms and restrictions of the trust[82] or invade principal[83] if no serious injury will result to the remaindermen. *Invasion* is usually permitted only when the cestui has an interest in the principal.[84] The extent of *deviation* would likely be limited by the operation of the prudent man rule.

In California, Civil Code Section 2261(4) empowers courts to permit deviation.[85] California courts seem to be strict, however, in allowing invasion or deviation. Authority to deviate may be granted on a showing of greatly changed conditions and strong equitable considerations, but benefit alone is not sufficient.[86] Invasion, on the other hand, will not be permitted in the absence of a clear expression in the trust instrument.[87] Suitable proceedings may properly be brought under Probate Code Section 1120.[88]

Courts in other jurisdictions have allowed deviation upon showing that an emergency has arisen threatening loss, that economic conditions have changed considerably due to unforeseen circumstances, that compliance would defeat or impair accomplishment of the purposes of the trust, or that

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(1948), where unborn beneficiaries were not bound by consent of those living (in accord with the weight of authority). *But cf.* Petition of Wolcott, 95 N.H. 23, 56 A.2d 641 (1948), where a needy widow was a strong enough factor to permit invasion although consented to by only the living remaindermen—the court willingly recognizing the decline in investment yields and purchasing power.

82 *E.g.*, St. Louis Union Trust Co. v. Ghio, ...Mo. App........, 222 S.W.2d 556 (1949); Citizens National Bank v. Morgan, 94 N.H. 284, 51 A.2d 841 (1947); Matter of Pulitzer, 139 Misc. 575, 249 N.Y.S. 87 (1931), *aff'd mem.*, 237 App. Div. 808, 260 N.Y.S. 975 (1932); RESTATEMENT, TRUSTS § 167; SCOTT, TRUSTS, *supra* note 13, § 167.1. See Scott, *Deviation from Terms of Trust*, 44 HARV. L. REV. 1025 (1931); Comment, 28 CALIF. L. REV. 785 (1940); Notes, 147 A.L.R. 815 (1943), 170 A.L.R. 1219 (1947).

In *In re* Stanford University (1936 Cal. Super.) 4 P-H TRUST SERV. ¶ 25,851 (1945), prior to the prudent man statute, the trustees of the university petitioned to invest part of the fund in stock as a hedge against inflation; held: since the primary purpose of the fund was to provide income to carry on the educational facilities intended by the donors, those investments would be permissible, if prudent men would make them.

83 RESTATEMENTS, TRUSTS § 168; SCOTT, TRUSTS, *supra* note 13, § 168; Note, 1 A.L.R. 2d 1328 (1948). The cases usually require that the accomplishment of the settlor's purposes or intent be found in the invasion. See Est. of Emerson, 139 C.A. 571, 34 P.2d 800 (1934); Wardens of St. Pauls Church v. Atty. Gen'l., 164 Mass. 188, 41 N.E. 231 (1895); Mills v. Mich. Trust Co., 124 Mich. 244, 82 N.W. 1046 (1900). *But cf.* Cassidy v. Murray, ... Me. ...., 68 A.2d 390 (1949); Cosgraves Will, 225 Minn. 443, 31 N.W.2d 20 (1948); Matter of Ely, 274 N.Y. 501, 10 N.E.2d 520 (1937). Invasion cases are also often classified as deviation cases.

84 RESTATEMENT, TRUSTS § 168.

85 "(4) Nothing in this section shall abrogate or restrict the power of the appropriate court in proper cases to direct or permit the trustee to deviate from the terms of the trust regarding the making or retention of investments."

86 Security First National Bank of Los Angeles v. Easter, 136 C.A. 691, 29 P.2d 422 (1934); *In re* Van Deusen's Estate, *supra* note 81 (dictum only). In Whittingham v. California Trust Co., 214 Cal. 128, 4 P.2d 142 (1931), deviation was allowed as no other person was affected. See Comment, 28 CALIF. L. REV. 785 (1940).

87 Estate of Markham, 28 Cal.2d 69, 168 P.2d 669 (1946).

88 "The trustee may also petition such court, from time to time, for instructions as to the administration of the trust . . . ." See *In re* Van Deusen's Est., *supra* note 81.