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Trusts -- Deviation from Investment Restrictions

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more important interest of the public in unimpeded access to newsworthy information. In the latter there should not be recovery; but it is objectionable that in the former this public interest is said to protect a publisher when such an interest is not present at all, simply because it might have been. It is submitted that upon finding a lack of legitimate public interest in the specific statements complained of, a court should base its decision on a further investigation of whether the defendant's intent was to commercially exploit plaintiff's private life.

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Trusts—Deviation from Investment Restrictions

In 1924 James B. Duke established the Duke Endowment when he transferred to trustees a large amount of securities, the income of which was to be used for educational, religious and other charitable purposes.[1] The trust indenture provided that the trustees could invest the funds of the trust in either government bonds or Duke Power Company securities, other investments being prohibited. In 1962 over 80% of the trust was invested in common stock of Duke Power, and over 95% of the remaining common stock was invested in two aluminum companies.[2] The trustees brought an action for modification of the trust instrument to permit them to invest in stocks and bonds of corporations other than Duke Power. Basing their opinion on New Jersey law because of the terms of the trust instrument,[3] the North Carolina Supreme Court said that a court

[1] 20% of net income is to be set aside until an additional $40,000,000 has been added to the trust. The remaining income is payable 32% to Duke University, 32% to such nonprofit hospitals in North and South Carolina as the trustees select, 5% to Davidson College, 5% to Furman University, 4% to Johnson C. Smith University, 10% to nonprofit organizations in North and South Carolina selected by the trustees which are engaged in caring for orphans, 2% for care of needy retired Methodist preachers, or widows and orphans of deceased Methodist preachers in North Carolina, 6% to be used in erecting rural Methodist churches in North Carolina, and 4% for maintenance and supervision of such churches. Cocke v. Duke Univ., 260 N.C. 1, 5-6, 131 S.E.2d 909, 911 (1963).

[2] Stocks in companies other than Duke Power were received from either Mr. Duke or his estate. In 1962 the number of shares and the values of aluminum company stocks held by the trust were as follows: 791,040 shares of Aluminum Ltd., of Canada, valued at $17,402,880; 639,644 shares of Alcoa common, valued at $35,180,420; 59,300 shares of Alcoa preferred, worth $5,040,500. *Id.* at 13, 131 S.E.2d at 916.

[3] The trust by its express language is "executed by a resident of the State

of equity may authorize a trustee to disregard the provisions of the trust instrument limiting his authority with respect to the kind of securities in which he may invest, but that the evidence in this case did not justify exercise of that power.[4]

The trustees could invest funds of the trust in either Duke Power securities or government bonds, neither of which appeared desirable to them. On the one hand they felt it would not be advisable, from a diversification standpoint, to purchase additional securities of Duke Power, because of the size of the trust's holding of that corporation's securities.[5] On the other hand, they felt it unwise to invest in fixed-dollar obligations since additional funds would be needed in the future to offset inflation and increasing population.[6] Thus, the trustees argued, neither government bonds nor Duke Power securities offered attractive investment potential for the trust fund; therefore they should be allowed to invest in securities of companies other than Duke Power to protect the beneficiaries and the objects of the trust.

The plaintiffs' evidence showed that since the creation of the trust the country has entered a period of general inflation which has not yet ended, and that the cost of higher education and hospital costs have increased and probably will continue to increase faster than average.[7] Officials of the beneficiary colleges projected large increases in enrollment as well as in educational costs per student in the future.[8] Trust investment experts testified that they were of the opinion that "proper safeguarding of the corpus of the Endowment requires a greater degree of diversification"[9] and "that the

of New Jersey in said State, is intended to be made, administered and given effect under and in accordance with the present existing laws of said State, notwithstanding it may be administered and the beneficiaries hereof may be located in whole or in part in other states, and the validity and construction thereof shall be determined and governed in all respects by such laws and statutes." *Id.* at 8, 131 S.E.2d at 913. See note 14, *infra,* for a discussion of other possible implications of this language.

[4] Cocke v. Duke. Univ., 260 N.C. 1, 131 S.E.2d 909 (1963).

[5] Also, a witness of the trustees had testified that Duke Power is now a mature company which cannot expect future expansion at a rate comparable to that of the past. *Id.* at 19, 131 S.E.2d at 921.

[6] There was evidence showing that the needs of the beneficiaries will continue to increase because of expanding population. *Id.* at 13, 131 S.E.2d at 917.

[7] Record, p. 151.

[8] Record, pp. 189-208.

[9] 260 N.C. at 14, 131 S.E.2d at 917.

restrictive investment provisions set forth in the Indenture constitute a threat to the safety of the Endowment corpus."[10]

The court referred to a New Jersey statute[11] and two cases in the New Jersey Court of Errors and Appeals[12] as "declaring the law which must be applied here."[13] Briefly stated, the law upon which the court relied holds that in order to change investment procedures in New Jersey, the trustee must show that because of changes in conditions not anticipated by the settlor, such a change would be necessary to avoid frustration of the purposes of the trust, and that the new investment policy would be advantageous to the purposes of the trust and to all beneficiaries. It would seem that the North Carolina court properly applied the present law of New Jersey in reaching its decision.[14] Although there was substantial evidence

[10] *Ibid.*

[11] N.J. STAT. ANN. tit. 3A, ch. 15, § 15(b) (1953), which reads in part: "If the court shall find that by reason of a change in conditions which occurs since the creation of the trust or which may be reasonably foreseen, the objects of the trust might be defeated in whole or in part by the investment... of all the funds of such trust in the kinds of investments to which the trustee is then limited by the statutes of this state or by the instrument... creating such trust and that the objects of the trust and the interests of all the beneficiaries thereof... would be promoted by the investment of all, or some part, of the trust fund otherwise, the court shall... authorize or direct the trustee ...to invest... in any class of investments, including common or preferred stocks of corporations...."

[12] Bliss v. Bliss, 126 N.J. Eq. 308, 8 A.2d 705 (1939); Reiner v. Fidelity Union Trust Co., 126 N.J. Eq. 78, 8 A.2d 175 (1939); *rev'd* 127 N.J. Eq. 377, 13 A.2d 291 (1940). In the *Bliss* case a large portion of the principal of a trust under a will was invested in railroad bonds; under the terms of the will the trustees could reinvest funds of the trust in legal securities. Both income and corpus diminished considerably, and the trustee sought permission to reinvest in common and preferred stocks, which were not legal trust investments. The court said that under the provisions of the will the trustee had broad investment power and denied authority to make the proposed investments because there was no evidence that the purposes of the trust were likely to be defeated if the required change were denied. In the *Reiner* case a trust's income was to be paid to the settlor's daughter; distribution of the principal to her was to be made over a period of years. Income from legal securities had shrunk from over $70,000 in 1925 to $54,000 in 1937, but there had been no substantial diminution of the principal. The court was asked to empower the trustee to invest portions of the trust fund in common stock. The court refused because there was no evidence that the purposes of the trust would have been defeated if the requested investments were not allowed.

[13] 260 N.C. at 8, 131 S.E.2d at 913.

[14] A question arises, however, as to whether or not *current* New Jersey law should have been applied in the case. The general rule governing the administration of an inter vivos trust is stated in RESTATEMENT, CONFLICT OF LAWS § 297 (1934), as follows: "A trust of movables created by

showing why it would have been advantageous to grant the requested relief, there was not sufficient evidence of the *necessity* of

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an instrument inter vivos is administered by the trustee according to the law of the state where the instrument creating the trust locates the administration of the trust." Comment *d* thereunder says, "In order to determine where the administration of the trust is located, consideration is given to the provisions of the instrument, the residence of the trustees, the residence of the beneficiaries, the location of the property, the place where the business of the trust is to be carried on." A majority of the trustees reside in North Carolina; most of the beneficiaries are located in North and South Carolina; the physical location of the securities held by the trust is in New York. Record, p. 206. The Endowment maintains two of its three offices in North Carolina. Thus, taking into consideration the elements set out above by the Restatement, it would seem that the trust would be administered according to the law of North Carolina, or possibly South Carolina or New York, nothing appearing in the trust instrument to the contrary. But the draftsman foresaw that a controversy might arise with respect to the administration of the trust and for that reason provided in the indenture that the trust was to be administered "in accordance with the *present existing* laws and statutes of [New Jersey]" (emphasis added). 260 N.C. at 8, 131 S.E.2d at 913. If this language be interpreted to mean that future administrative acts be according to the law of New Jersey as of the date of each act, then it would appear that the court properly based the decision on the statute and two subsequent cases, since the statute would apply to trusts created before its passage. See Reiner v. Fidelity Union Trust Co., 126 N.J. Eq. 78, 8 A.2d 175 (Ch. 1939). But if the language be interpreted as requiring that the trust be administered according to the laws of New Jersey at the time of the creation of the trust, then the statute and above cases would not seem to be authority on which to base the decision, because the trust was created in 1924, thirteen years before the statute passed and long before the cases were decided by the Court of Errors and Appeals. Under this interpretation it would seem that the settlor, in effect, included in the indenture his own rules governing administration of the trust, to be used wherever the trust was being administered. To put it another way, he incorporated by reference into the trust indenture the 1924 laws of New Jersey, which became part of the indenture itself. Thus it would appear that a subsequent New Jersey statute would have no effect upon it. This point was raised by the defendants, Brief for Defendants, pp. 39-43, but the court did not explain why it held that the statute and cases declared "the law which must be applied here."

Apparently courts of chancery in New Jersey had jurisdiction in 1924 to permit investments of trust funds in securities other than those allowed by the trust instrument. See Price v. Long, 87 N.J. Eq. 578, 101 A. 195 (1917). Two later cases have said that courts of equity have always had the inherent authority to do so. Morris Community Chest v. Wilentz, 124 N.J. Eq. 580, 3 A.2d 808 (1939); New Jersey Nat'l Bank & Trust Co. v. Lincoln Mortgage and Title Guar. Co., 105 N.J. Eq. 557, 148 A. 713 (1930). But the court could exercise the power only in an emergency, where the circumstances required that something be done. Price v. Long, *supra*. Thus the 1937 statute and subsequent cases, though perhaps incorrectly applied in the principal case, have not significantly changed the law in this area, and under the law prevailing in New Jersey at the time the trust was created a similar result probably would have been reached.

doing so. It was on this ground that the court granted the motion for nonsuit.

The instant case would seem to fall within the scope of the generally accepted doctrine that equity has no authority to alter a trust merely to improve a settlor's gift to the beneficiaries.[15] Under this view the power to permit deviation by the trustee should be limited to emergency situations that threaten the purposes of the trust. The general principle being acknowledged, the critical question is what circumstances actually do create an emergency warranting deviation. An interesting comparison to the principal case is afforded by two fairly recent cases, *Stanton v. Wells Fargo Bank & Union Trust Co.*[16] and *In re Trusteeship under Agreement with Mayo.*[17]

In the *Stanton* case the trust instrument executed in 1930 provided that investments by trustees should be made only in bonds of the federal government, states or municipalities, or in corporate bonds rated at least "AA" by Moody's Investment Service.[18] Total dollar values of the trust in the following years were as follows: 1931—3,460,516 dollars; 1936—2,323,719 dollars; 1954—2,860,687 dollars.[19] Income in 1938 was 88,891 dollars and in 1954 was 109,943 dollars.[20] The plaintiff felt that the evidence showed a marked decline in the purchasing power of the dollar and the return on bonds (as compared to the return on common stocks). However, the court observed that there was no evidence of any beneficiary's being in want, or of the distributable income being insufficient to supply the reasonable needs of all the beneficiaries. The court admitted that inflation had occurred in the past, but said that no one knows whether or not it will continue in the future. The court felt it should not try to guess what economic conditions might be in the future by permitting the deviation where no real need or emergency was shown, and refused to allow deviation.

[15] See, *e.g.*, Rogers v. English, 130 Conn. 332, 33 A.2d 540 (1943); Porter v. Porter, 138 Me. 1, 20 A.2d 465 (1941); Thomson v. Union Nat'l Bank, 291 S.W.2d 178 (Mo. 1956); John A. Creighton Home v. Waltman, 140 Neb. 3, 299 N.W. 261 (1941); Toledo Trust Co. v. Toledo Hosp., 174 Ohio St. 124, 187 N.E.2d 36 (1962); RESTATEMENT (SECOND) TRUSTS § 167, comment *c* (1959); 3 BOGERT, TRUSTS AND TRUSTEES § 561 (1946).

[16] 150 Cal. App. 2d 763, 310 P.2d 1010 (1957).

[17] 259 Minn. 91, 105 N.W.2d 900 (1960).

[18] Stanton v. Wells Fargo Bank & Union Trust Co., 150 Cal. App. 2d 763, 766, 310 P.2d 1010, 1012 (1957).

[19] *Id.* at 767, 310 P.2d at 1013.

[20] *Id.* at 771, 310 P.2d at 1016.

In the *Mayo* case there were two trusts set up—one in 1917 and the other in 1919. The donor died in 1939. The investment provisions of both said the following: "The TRUSTEES shall . . . manage, care for and protect said fund all in accordance with their best judgment and discretion, invest and re-invest the same in real estate mortgages, municipal bonds or any other form of income bearing property (but not real estate or corporate stock) . . . ."[21] The value of the assets of the larger trust was $957,712 in 1940 and $968,893 in 1958; but due to inflation the value of the trust in terms of 1940 dollar values was only $456,140 at the later date.[22] That is, the actual value of the trust fund, in terms of purchasing power, had been cut almost in half since 1940, due to inflation. A similar decline in purchasing power had taken place in regard to the smaller trust. The court said that unless deviation was ordered the dominant intention of the donor to prevent a loss of the principal would be frustrated; and that unless deviation be allowed, the assets of the trusts within the next twenty years would be worth less than one-fourth of their value at the time of the donor's death. Another factor considered was that stocks are now sounder investments than they were at the time the trust was created, due to increased government and exchange regulations and improved management. The court felt that the trustees should have the right to deviate from the restrictive provisions of the trust and permitted them to invest a reasonable amount of the trusts in corporate stocks. In this way the trusts were to be fortified against inflation.

When the court in the *Mayo* case found that the dominant intention of the donor was to prevent a loss in the principal, it provided itself with a necessary fact upon which to base its decision.[23] Also it would seem that the court was sensible in recognizing that inflation decreases the value of the principal even though its value in dollars does not decrease, and in recognizing the probability of

[21] 259 Minn. at 92-3, 105 N.W.2d at 902.

[22] *Id.* at 93, 105 N.W.2d at 902.

[23] In Toledo Trust Co. v. Toledo Hosp., 174 Ohio St. 124, 187 N.E.2d 36 (1962), the plaintiff relied upon the *Mayo* case in seeking to deviate from the investment provisions of the trust instrument because inflation had devalued the purchasing power of the dollar. In denying relief the court said, "The court in the Mayo case reached these two conclusions by first concluding that the dominant intention of the testator was to preserve the corpus of the trust. It is difficult for this court to reach that conclusion under this trust. . . ." *Id.* at 127, 187 N.E.2d at 39.

future inflation. Because of the facts found in *Stanton,* there was no basis upon which to hold that the purpose of the trust was threatened, and so the court could not grant relief. It is regrettable that the court in *Stanton* took the narrow view prohibiting recognition of future inflation, because this approach seems to ignore a strong economic trend of recent years which is generally expected to continue.[24] Although the trust in the principal case was charitable rather than private,[25] the facts of that case would seem to be more in line with the *Stanton* case than with *Mayo,* since there were not sufficient findings of substantial danger to the accomplishment of the trust purpose. Although the investment provisions do not seem to be the best possible, this alone is not a sufficient ground to change them under general trust principles and the laws of New Jersey. In spite of this, a slightly different emphasis by the court would have allowed a more advantageous holding without violating established trust principles. The court could have found justifiably that the trust's purposes were substantially endangered by the investment restrictions. From the settlor's instructions to add part of the income to the principal, the court could have plausibly concluded that the settlor's main intention was either to prevent loss of the principal or to increase the size of the trust fund. Under either conclusion his intention could have been defeated because of the great imbalance of investments which subjects the trust to undue risk. If the court felt the latter to be his intention, it could have reasonably determined that the investment restrictions would retard the growth of the trust fund, thereby defeating the settlor's intention partially or wholly. Likewise, the court could have determined that the investment restrictions would prevent growth of the trust fund at a rate sufficient to meet the beneficiaries' needs in the future, when additional funds would be necessary because of increased population and inflation, thereby thwarting the settlor's obvious intention to fulfill their needs. Thus, as was done in *Mayo,* the court could have furnished

[24] "Among the few things which economists predict with any degree of confidence is that—with some possible exceptional periods—prices will, on the average, be higher in future decades than they are today." *Why Prices Stay Up,* Nation's Business, Feb., 1963, p. 64. But see Upgren, *The American Economy: 1933 to 1973,* 17 J. AM. SOC'Y C.L.U. 329 (1963).

[25] Since the typical charitable trust is intended to last a very long time, it is reasonable and necessary to allow the trustee more flexibility than in the case of private trusts. See 4 POWELL ON REAL PROPERTY 488 § 579 (1954).

itself with a basis upon which to hold that the trust purposes were endangered, thereby fulfilling the requirement necessary to allow deviation under existing law.

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Wills—Incorporation by Reference—Invalid Instruments

In *Godwin v. Wachovia Bank & Trust Co.*[1] husband and wife executed a trust agreement which the court conceded to be void as an inter vivos trust because of the draftsman's failure to obtain and certify a private examination of the wife as required by section 52-12 of the General Statutes. Both husband and wife executed wills of even date with the trust instrument, each disposing of his property as provided in the trust agreement. After the wife's death the husband executed a new will which differed substantially from the terms of the trust agreement. In an action by the trustee seeking specific performance of an alleged contract between husband and wife to will their property according to the terms of the trust agreement, the court held that the trust agreement was incorporated in the respective wills by reference; that the wills themselves established the existence of the alleged contract; and that the trustee was entitled to specific performance for the benefit of the beneficiaries named in the original wills.

The doctrine of incorporation by reference[2] is recognized in England and in a great majority of American jurisdictions.[3] Four fea-

[1] 259 N.C. 520, 131 S.E.2d 456 (1963).

[2] This doctrine should not be confused with the closely related doctrine of "facts of independent legal significance." Professor Scott states, in reference to the latter doctrine, that: "[A] disposition made in a will is not invalid although its terms do not fully appear in the will, if those terms can be ascertained from facts which have significance apart from their effect upon the disposition in the will. The existence of a trust at the time of the testator's death, created by him at some time prior to his death, is such a fact. *It is not the trust instrument, but the trust itself, which has independent significance.*" 1 SCOTT, TRUSTS § 54.3, at 367 (2d ed. 1956). (Emphasis added.)

Since a valid inter vivos trust was never created here, and the trust instrument cannot be a fact of independent significance, this doctrine would seem inapplicable.

[3] ATKINSON, WILLS § 80, at 385 nn. 4-5 (2d ed. 1953), and cases cited therein. The doctrine is stated thusly in Newton v. Seaman's Friend Soc'y, 130 Mass. 91, 93 (1881): "If a will, executed and witnessed as required by statute, incorporates in itself by reference any document or paper not so executed and witnessed, whether the paper referred to be in the form of a will or codicil, or of a deed of indenture, or of a mere list or memoran-