

STATUTORY NOTE

TRUSTEE INVESTMENT—LEGAL LIST

The law of trustee investment has developed in a chameleonic fashion; most courts following one rule at first, then changing to another, and finally reverting to their original position. Historically two standards developed for trustee investments. The "prudent-man rule" was enunciated first, with the "legal list rule" coming many years later. In early English law the court set the standards for trustee investment or held that the conduct of a prudent man was the standard.¹ The English courts first held that only government obligations and first mortgages on realty were legal investments.² This rule was followed by a few cases in the United States,³ but the great majority of early United States cases followed the rule in the case of *Harvard College v. Armory*.⁴ This case laid down the so-called "prudent-man rule."⁵ The rule, as stated by the court was:

All that can be required of a trustee to invest, is, that he shall conduct himself faithfully and exercise a sound discretion. He is to observe how men of prudence, discretion, and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested.⁶

This standard gave the trustee an extremely broad power of investment and appealed to many courts.⁷

Thirty-nine years after the *Harvard College* decision⁸ the "legal list rule" was "born," in the case of *King v. Talbot*.⁹ In that case the court said that the trustee should act as a prudent man would act in handling his own affairs. The court then articulated what a prudent man should invest in, and limited investments to things with a fixed maturity and

1. BOGERT, *LAW OF TRUSTS* 271 (4th ed. 1963).

2. *Ex Parte Cathorpe*, 1 Cox Eq. Cas. 182 (1785).

3. *Appeal of Hemphill*, 18 Pa. 303 (1832); *Simmons v. Oliver*, 74 Wis. 633, 43 N.W. 561 (1889).

4. 26 Mass. (9 Pick.) 446 (1830).

5. 3 SCOTT, *LAW OF TRUSTS* 1669 (2d ed. 1956).

6. *Supra* n. 4 at 461.

7. *Peckham v. Newton*, 15 R.I. 321, 4 A. 758 (1886); *Sheets v. J. G. Flynt Tobacco Co.*, 195 N.C. 149, 141 S.E. 355 (1928); *Scoville v. Brock*, 81 Vt. 405, 70 A. 1014 (1908); *Kimball v. Whitney*, 233 Mass. 321, 123 N.E. 665 (1919); *Brown v. French*, 125 Mass. 410, 28 Am. Rep. 254 (1878).

8. *Supra* n. 4.

9. 40 N.Y. 76 (1869).

predetermined rates of return.¹⁰ By this reasoning, the court prohibited a trustee from investing in stocks. Under this rule, trustee investments were strictly limited. This limited power over the trustee appealed to legislatures prompting them to pass acts authorizing investments according to "legal lists." The legal lists became so popular that most states discarded the "prudent-man rule." In the 1940's however, most states took an "about-face" and reverted once again to the "prudent-man rule."¹¹

There are two types of legal lists—mandatory and permissive. A mandatory list prohibits absolutely any deviation from the list.¹² A permissive list lets the trustee deviate to a certain extent. The court determines whether a list is mandatory or permissive by the words used in the list. If the words "shall invest" appear, the list is mandatory. If the trustee invests outside this list, he has committed a breach of trust regardless of whether he was prudent or not.¹³ When the words "may invest" appear, the list is called a permissive list. Any investment outside this list protects the trustee if he acted as a prudent man.¹⁴

The distinction drawn between a permissive and mandatory legal list seems to indicate that there is really no difference between the permissive list and the "prudent-man rule." This is not the case, however, because there is a decided difference between the two. The "prudent-man rule" offers no specific guide to the trustee investor. The permissive legal list gives to the trustee a minimum of authorized investments, and when he invests in these, there is no question as to his prudence *vel non*.

Before the Georgia Code was enacted, Georgia applied the "prudent-man rule."¹⁵ The current Georgia standard for trustee investments is the legal lists. This list not only applies to executors and administrators, but also to guardians.¹⁶ The legal list is found in several sections throughout the Code.¹⁷ The sections comprising the list use the words "shall" and

10. *Id.* at 87.

11. *Supra.* n. 1.

12. Comment, 49 YALE L. J. 896 (1940).

13. *In re Trusteeship of First Minneapolis Trust Co.*, 207 Minn. 187, 277 N.W. 899 (1938); *In re Smith*, 279 N.Y. 479, 18 N.E.2d 666 (1939); *Humphries v. Manhattan Savings Bank and Trust Co.*, 174 Tenn. 17, 122 S.W.2d 446 (1938).

14. *Clark v. Beers*, 61 Conn. 87, 23 A. 717 (1891); *In re Cook's Trust Estate*, 20 Del. Ch. 123, 171 A. 730 (1934); *Buckle v. Marshall*, 176 Va. 139, 10 S.E.2d 506 (1940).

15. *Brown v. Wright*, 39 Ga. 56 (1869); *Moses v. Moses*, 50 Ga. 9 (1873).

16. *Marshall v. Citizens & Southern Nat'l Bank*, 50 Ga. App. 123, 187 S.E. 240 (1936).

17. GA. CODE ANN. §108-417 (1959 rev.) (Investment in bonds and other securities); §108-418 (Investment in land); §108-419 (Investment in State securities at less than 7%); §108-420 (Investments in validated county, municipal, or school district bonds); §108-421 (Investment in farm loan bonds issued by Federal land banks or joint-stock land banks); §109-512 (Deposits of trust funds at interest with bank or trust company covered by Federal Deposit Insurance as legal investments); §109-513 (Deposit by bank or trust company of trust funds with self);

"may" invest, which raises the problem as to whether Georgia's legal list is permissive or mandatory. No Georgia case has ever expressed a view directly in point, but a reading of the words used in the list seems to indicate a legislative intent to make the list mandatory rather than permissive.¹⁸ Several Georgia cases also seem to express the view indirectly that the Georgia legal list is mandatory rather than permissive.¹⁹ In *Brown v. Wright*,²⁰ a guardian invested in securities not on the legal list. The court said that a guardian investing in stocks and bonds not on the list does so at his own risk and he is liable for the value of such investment at the time of such investment.²¹ In another Georgia case, *Georgia Railroad Bank and Trust Co. v. Liberty National Bank and Trust Co.*,²² a guardian had invested his ward's funds in non-legal bonds. The court said that if a guardian did this without first obtaining a court order, it was against the law and a subsequent guardian could sue the guardian-investor for the amount he invested.²³ A leading Georgia scholar says that a guardian investing outside the legal list and without a court order, does so at his own risk.²⁴

Georgia is one of the few states that still follow a legal list. An overwhelming majority of the states have adhered to the "prudent-man rule."

§109-514 (No authority necessary for deposit); §109-603 (Right of trust institution to invest in common trust funds); §109-606 (Trust instrument; effect of limitation to legal investments); §109-607 (Trust instrument; effect of provision for investment in common trust fund, or in other than legal investments, or of giving discretion to fiduciary); §109-608 (Limitation of investment for one estate); §113-1517 (Investment in land); §113-1518 (Investment in State bonds and other securities; insured deposits; retention of property of estate); §113-1519 (Investment in State bonds and other securities; return to ordinary); §113-1520 (Investments in validated county or municipal bonds); §49-215 (Investment in securities issued by State or United States; return; interest); §49-216 (Investment in land); §49-217 (Investment in State securities at less than 7%); §49-218 (Investments in validated county or municipal bonds); §89-816.1 (Investment of surplus, or of funds not immediately needed, in United States war bonds or other obligations); §87-701 (Authority of municipality to invest; time for investment); §87-702 (Investment of funds on hand by municipalities); §87-703 (Investment in city's own bonds; order of payment of bonds); §87-706 (Investment by counties in bonds of county, State, or United States); §2-5609 (Investment of State sinking fund); §16-437 (Shares of associations as investment of trust funds); §99-1136 (Bonds as legal investments); §99-1162 (Bonds for war housing projects as security for public deposits and as legal investments); §98-216 (Bonds as legal investments for trustees and as lawful deposits of securities with public officers); §78-520 (Veterans Resettlement Corporation revenue bonds).

18. GA. CODE ANN. §108-417 (1959 rev.) "Any other investments of trust funds shall be made under an order of the superior court, either in term or granted by the judge in vacation, or else at the risks of the trustee. . . ."

19. *Little v. Haas*, 68 F. Supp. 545 (1946); *Clark v. Clark*, 167 Ga. 1, 144 S.E. 787 (1928); *Mobley v. Phinizy*, 42 Ga. App. 33, 155 S.E. 73 (1930); *Rogers v. Dickey*, 117 Ga. 819, 45 S.E. 71 (1903).

20. *Supra* n. 15.

21. *Id.* at 101-102.

22. 180 Ga. 4, 177 S.E. 803 (1934).

23. *Ibid.*

24. REDFERN, WILLS AND ADMINISTRATION OF ESTATES IN GEORGIA 631 (rev. 1938).

The advocates of the "prudent-man rule" say that it is more flexible and enables the trustee to take advantage of changing conditions.²⁵ It frees the trustee from a so-called "legislative straight jacket" placed on him by the legal lists.²⁶ Despite these advantages of the "prudent-man rule", this standard leaves the trustee-investor in a very unsure position. He does not know if his investment is legal until a jury decides whether or not he has been a prudent man. The legal lists have made the position of the trustee-investor more certain than at common law.²⁷ The trustee needs some specific standard to follow when making investments, and the legal list has given him this standard. The attack on the inflexibility of legal lists is perhaps well founded as to the mandatory type, in that the list is too restrictive on the trustee. The preferable standard is the permissive legal list. The permissive list gives the trustee a standard to go by, and remains flexible enough so that the trustee who goes outside the list will not be liable for breach of trust if he acted as a prudent investor.²⁸

If the trustee has a permissive list to guide him he will be more inclined to invest. He can be sure that by following the list, he will not be held personally liable for a breach of trust. Yet, if the trustee does invest outside the list, he may still be absolved from liability if he acted prudently. The permissive legal list, by fostering investments in this fashion, appears to be the best way to secure to the beneficiary of the trust the maximum benefit of the trust, and still offer the trustee some protection by giving him some specific standard to guide his conduct.

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25. Comment, 15 ALA. L. REV. 99, 100 (1962).

26. Comment, 49 YALE L. J. 906 (1940).

27. Note, 49 HARVARD L. REV. 825 (1936).

28. *Supra* n. 14.

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