

TRUSTS—TRUSTEE INVESTMENTS—THE RETURN OF THE PRUDENT INVESTOR RULE

The “prudent investor rule” for trust investment was reintroduced in Georgia in 1972.¹ This marked a return to the standard employed prior to the adoption of the first Georgia Code in 1873. In the interim period, 1873-1972, the so-called legal list standard was the guide for trustees investing under fiduciary instruments created in Georgia.² It has been suggested that: “One needs an excuse for adding anything at all to the very considerable volume of comment about the prudent man rule for trust investment.”³ The chief purpose of this writing is to delineate the distinction between the “prudent investor rule” and the legal list criterion, and to set forth some observations concerning Georgia’s new law, entitled “Executors and Trustees—Investments Authorized” (hereinafter referred to as the Act).

The transition from the “legal list rule” to the prudent investor standard is entirely in accord with the modern trend in fiduciary investments. Georgia, in fact, was one of the few jurisdictions still preserving a statutory or legal list approach to trustee administration.⁴ A prior note, *Trustee Investment—Legal List*, set forth a concise presentation of trustee investment in Georgia under the legal list standard.⁵ A feature in that article was a compilation of the then extant legal list as found in the various sections of the code. That compilation must be revised to include legislation passed since 1964 before commencing the present discussion.⁶ This revision is needed since section 5 of the Act, makes its

1. Ga. Laws, 1972, p. 450.

2. *Moses v. Moses*, 50 Ga. 9 (1873).

3. Stevenson, *Why The Prudent Man*, 7 VAND. L. REV. 74 (1953).

4. Horowitz, *Uniform Trustees' Powers Act*, 41 WASH. L. REV. 1 (1966); Shattuck, *The Development of the Prudent Man Rule for Fiduciary Investment in the United States in the Twentieth Century*, 12 OHIO ST. L. J. 491 (1951); G. BOGERT, *LAW OF TRUSTS* 271 (4th ed. 1963).

5. 15 MERCER L. REV. 530 (1964).

6. This list represents a compilation of the legal investment statutes created before 1964 and set forth in 15 MERCER L. REV. 530 (1964) and the legal investment statutes approved since that date. All citations within this footnote are to sections of GA. CODE ANN.: investment of state sinking fund, § 2-5609 (Rev. 1948); shares of associations as investment of trust funds, §§ 16-437 to -438 (Rev. 1971); bonds issued by the University System Building Authority, § 32-120a (Rev. 1969); investment in securities issued by state or United States (return interest) § 49-215 (Rev. 1965); investments in land, § 49-216 (Rev. 1965); investment in state securities at less than seven per cent, § 49-217 (Rev. 1965); investment in validated county or municipal bonds, § 49-218 (Rev. 1965); investment in bonds of urban redevelopment agencies or housing authorities, § 69-1111 (Rev. 1972); authority of municipality to invest, time for investment, § 87-701 (Rev. 1971); investment of proceeds of bonds issued by political subdivisions, § 87-701a (Rev. 1971); investment of funds on hand by municipalities, § 87-702 (Rev. 1971); investment in city's own bonds, § 87-703

provisions applicable only to investments made under instruments created after July 1, 1972.⁷ Accordingly, the present legal list will be of importance to the investor for an indeterminate period, since investors will be operating under a dual system depending on the creation date of the applicable instrument.

The legal list standard, often referred to as the English Rule⁸ or New York Rule,⁹ evolved from Victorian days in England where the trustee was to act as a conservator, not as a manager. Most authorities concur that the New York case, *King v. Talbot*,¹⁰ has become the keystone decision for jurisdictions supporting the "legal list rule."¹¹ Fiduciary investments under the standard are limited by statute to a prescribed list of legals approved by the state legislature. These statutory lists may either be permissive or mandatory. If the list is permissive, and investments are made outside the list, the investor must sustain the burden of

(Rev. 1971); investment by counties in bonds of county, state, or United States, § 87-706 (Rev. 1971); investment of surplus, or of funds not immediately needed, in United States war bonds or other obligations, § 89-816.1 (Rev. 1971); investment in State Bridge Building Authority bonds, § 95-2329 (Rev. 1972); investment in bonds of Georgia Rural Roads Authority, § 95-2630 (Rev. 1972); bonds as legal investments for trustees and as lawful deposits of securities with public officers, § 98-216 (Rev. 1968); bonds as legal investments, § 99-1136 (Rev. 1968); bonds for war housing projects as security for public deposits and as legal investments, § 99-1162 (Rev. 1968); bonds of State Hospital Authority, § 99-1420 (Rev. 1968); investment in bonds and other securities, § 108-417 (Supp. 1971); investment in land, § 108-418 (Rev. 1959); investment in state securities at less than seven per cent, § 108-419 (Rev. 1959); investment in validated county, municipal, or school district bonds, § 108-420 (Rev. 1959); investment in farm loan bonds issued by federal land banks or joint-stock land banks, § 108-421 (Rev. 1959); investment by fiduciaries in real estate loans, § 108-450 (Supp. 1971); investment in property outside of Georgia, § 108-605 (Supp. 1971); deposits of trust funds at interest with bank or trust company covered by federal deposit insurance as legal investments, § 109-512 (Rev. 1959); deposit by bank or trust company of trust funds with self, § 109-513 (Rev. 1959); no authority necessary for deposit, § 109-514 (Rev. 1959); right of trust institution to invest in common trust funds, § 109-603 (Rev. 1959); trust instrument, effect of limitation to legal investments, § 109-606 (Rev. 1959); trust instrument, effect of provision for investment in common trust fund, or in other than legal investments, or of giving discretion to fiduciary, § 109-607 (Rev. 1959); limitation of investment for one estate, § 109-608 (Rev. 1959); delivery to common trust fund as money, securities not readily saleable at the price, § 109-622 (Supp. 1971); limitation on investment by trust institution, § 109-905 (Supp. 1971); investment in land, § 113-1517 (Rev. 1959); investment in state bonds and other securities, § 113-1518 (Supp. 1971); investment in state bonds and other securities, return to ordinary, § 113-1519 (Rev. 1959); investment in validated county or municipal bonds, § 113-1520 (Rev. 1959).

7. Ga. Laws, 1972, p. 450. This is in accord with the general rule that such statutes do not apply retroactively. A. SCOTT, *LAW OF TRUSTS* § 227.13, at 1843 (3d ed. 1967).

8. Shattuck, *supra* note 4.

9. 15 ALA. L. REV. 79 (1962).

10. 40 N.Y. 76 (1869).

11. Barclay, *Why The Prudent Man Rule*, 99 TRUSTS & ESTATES 127 (1960); Shattuck, *The Massachusetts Prudent Man In Trust Investments*, 25 BOSTON L. REV. 307 (1945).

proving the use of reasonable care and skill. If the list is mandatory, it is generally thought that an investment outside the list would be a breach of trust regardless of the investor's prudence.¹²

The "prudent investor rule," an invention of the American courts, was first enunciated by Mr. Justice Putnam in the widely cited case of *Harvard College v. Amory*.¹³ Not unlike the legal list criterion, the standard has been billed under various titles, *i.e.*, The American Rule¹⁴ and The Massachusetts Rule.¹⁵ Statutes prescribing the rule engendered wide approval beginning about 1940.¹⁶ The rule gives the trustee power to act where, in the exercise of prudence, he deems action necessary. The standard adds resiliency and adaptability in trust administration and discourages reliance on mechanical guidelines by permitting constant adjustment in investment powers to the needs of the trust.¹⁷ Informed and intelligent trustees are given an opportunity to hedge against the possibility of destructive inflation.¹⁸

The reader is reminded, as a reference point, that the trustee in the performance of his duties is governed, first, by the instrument creating the trust, second, by the statutes of the state, and third, by the law as set forth in the decisions of the courts. Sections 3 and 4 of Georgia's new Act are in keeping with this reasoning.¹⁹

Different questions of statutory interpretation have developed in other jurisdictions depending on the variation of the "prudent investor rule" embodied in the particular state's statute.²⁰ Georgia's version is no exception. First, is the statute applicable only to executors and trustees to the exclusion of guardians? The answer must be in the affirmative. The preamble to the Act and sections 1 and 5 refer only to executors and trustees, suggesting the exclusion of other fiduciaries.²¹ This exclusion is not without precedent or foundation. Similar statutes in other states have been made applicable only to banks and trust companies, others to all trustees, and some to all fiduciaries.²² In Georgia, past legal listing statutes have been careful to either include guardians or

12. G. BOGERT, *supra* note 4, at 270; *see also* 15 MERCER L. REV. 530 (1964).

13. 9 Pick 446 (Mass. 1830); Shattuck, *supra* note 4, at 506.

14. King, *The Meaning of the "Prudent Man Rule,"* 24 ROCKY MT. L. REV. 44 (1952).

15. Shattuck, *supra* note 11.

16. G. BOGERT, *supra* note 4, at 281.

17. Horowitz, *supra* note 4, at 7.

18. King, *supra* note 14, at 51.

19. Ga. Laws, 1972, p. 450.

20. A. SCOTT, *supra* note 7, at 1842.

21. Ga. Laws, 1972, p. 450.

22. A. SCOTT, *supra* note 7, at 1843.

exclude them in their operation. Moreover, guardians have traditionally been more closely regulated by statute than executors and trustees, and the tendency of the courts appears to be to hold guardians strictly to their duties as defined by statute.²³ The conclusion must be that Georgia's version of the prudent investor statute is applicable only to executors and trustees, and guardians will continue to be governed by the appropriate legal list. The legal list for guardians is presently found in several different titles of the code.²⁴

Section 6 of the Act repeals all laws in conflict with the new standard.²⁵ This is not to be construed as repealing the previously enacted legal lists.²⁶ There has been some question of whether the past legal lists in Georgia were mandatory or permissive.²⁷ Retaining the collective list as permissive rather than repealed by the Act will render this issue virtually moot. The logic for retention is founded in the following considerations. We have not seen the last legal listing. It is anticipated that acts creating new revenue raising measures will continue to note that they are acceptable for investment purposes. This procedure has been adopted by two neighboring states with similar standards in that each state has continued to create new legislation listing certain investments as acceptable subsequent to the passage of "prudent investor rule" statutes.²⁸ Mr. William Fratcher, a noted writer in the field, reveals that many jurisdictions maintain both permissive legal lists and a prudent investor statute.²⁹ It is clear that section 6 of the Act does not repeal the present legal listings; instead, they are retained as permissive.

At first blush it may appear that the above conclusion merely indicates that Georgia now has a permissive legal list standard, but there is a noteworthy distinction between a prudent investor standard and a permissive legal list guide. The distinction concerns the burden of proof where there is an alleged breach of a fiduciary's duty. Under a "prudent

23. *Georgia R.R. Bank & Trust Co. v. Liberty Nat'l Bank & Trust Co.*, 180 Ga. 4, 177 S.E. 803 (1934); *Brown v. Wright*, 39 Ga. 96 (1869); see note 5 *supra*, at 532.

24. The present legal lists for guardians are found in the following sections of GA. CODE ANN.: §§ 49-215 to -218 (Rev. 1965); § 69-1111 (Rev. 1967); §§ 95-2329, -2630 (Rev. 1972); § 98-216 (Rev. 1968); §§ 99-1136, -1162, -1420 (Rev. 1968); § 108-421 (Rev. 1959); §§ 109-512 to -514 (Rev. 1959); and § 113-1518 (Supp. 1971).

25. Ga. Laws, 1972, p. 450.

26. Chaffin, *Recent Developments In Georgia Fiduciary Law: An Update on Legislation and Litigation*, 9 GA. ST. B.J. 9, 11 (1972).

27. For the view that Georgia's legal lists are mandatory, see note 5 *supra*, at 531, 532; but see G. BOGERT, *supra* note 4, at 271, for the view that Georgia's legal lists are permissive.

28. See ALA. CODE ANN. § 58-47 (Rev. 1958); FLA. CODE ANN. § 18.11 (Rev. 1969); and subsequent enactments in these respective codes as illustrative.

29. Fratcher, *Trustees' Powers Legislation*, 37 N.Y.U. L. REV. 627, 635 (1962).

investor rule" statute the party *challenging* the prudence of an investment has the burden of demonstrating lack of propriety regarding the investor's decision. This is true even where, as in Georgia, legal lists are retained and the investment is not listed as a "legal." In contrast, under the permissive legal list standard the fiduciary has the burden of establishing the prudence of a challenged investment not designated as "legal." The consequence of this distinction in Georgia, with its combination legal list and "prudent investor rule" statutes, is to place the burden of proof on the challenger in any action questioning the prudence of an investment.

The significance of this newly approved legislation can be couched in the following terms. The departure from the legal list criterion does not open the trust fund to speculation or increased risk. As one writer stated, "The prudent man rule is definitely not a *carte blanche* authority to invest in anything a trustee chooses."³⁰ Nevertheless, executors and trustees may now take advantage of new forms of investment on an equal footing with other investors rather than waiting for the state legislature to act. The Act creates more flexibility in investing because the executor or trustee is no longer confined to a restricted list of legals. They may on their initiative seek new investment opportunities. The new standard brings Georgia in line with the decided majority of other states in this area of trust administration, and should prove beneficial to out-of-state administrators investing funds derived from a Georgia trust. There have long been strong supporters³¹ of the "prudent investor rule" and more recently some detractors.³² Doubtless, each viewpoint has merit, but the reasoning espoused by the former appears more enlightened and the return of the standard in Georgia is welcomed.

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30. Barclay, *supra* note 11, at 128.

31. 23 WASH. L. REV. 78 (1948); Stevenson, *supra* note 3; Shattuck, *supra* note 4; Barclay, *supra* note 11; Fratcher, *supra* note 29.

32. McSwain, *The Prudent Man Rule*, 106 TRUSTS & ESTATES 742 (1967).

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