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Advancing the Law—What’s Behind Those New Uniforms:

Uniform Prudent Management of Institutional Funds Act
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I. Introduction and Background

Uniform Management of Institutional Funds Act (UMIFA 1972)

- Provides guidance on investment authority
- Permits delegation of authority to independent financial advisors
- Authorizes expenditure of appreciation of investment funds
- Provides rules for the release of restrictions on the use or investment of funds
- Enacted in 47 jurisdictions

Revised UMIFA → UPMIFA

Emphasis on Prudence

Trusts and Nonprofit Corporations

- Standards on investment are merging
- Standards should be – and probably already are – the same
- UPMIFA still applies to nonprofit corporations, not to most trusts
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II. Definitions – What Does the Act Cover?

Endowment Fund

- Not wholly expendable on a current basis
- Not board-designated funds

Institution

- Organized and operated exclusively for charitable purposes (a charity)

Institutional Fund

- A fund held by an institution (i.e., by a charity)
- Not a fund held by a trustee that is not an institution (a corporate trustee or an individual trustee), so most trusts are excluded
- Not assets held primarily to accomplish a charitable purpose and not primarily for investment (“program-related assets”)
- Not a split-interest trust until after the noncharitable interest terminates

III. Standard for Managing and Investing Institutional Funds

UPMIFA Provides Better Guidance than UPMIFA

- UPMIFA does not adopt a “trust” standard
- UPMIFA combines language from the Revised Model Nonprofit Corporation Act and the Prudent Investor Act to clarify that the standard is neither a corporate nor a trust standard and instead is a charitable standard

RMNCA

“in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances”

Prudent Investor Act - Factors

- Gift instrument – donor intent
- Incur only reasonable costs
- Reasonable effort to verify facts
- General economic conditions
- Possible effect of inflation or deflation
- Expected tax consequences
- Role of each investment in overall portfolio
- Expected total return
- Other resources
- Needs of institution to make distributions and preserve capital
- Asset’s special relationship to institution’s purposes
- Overall investment strategy – portfolio approach
- Duty to diversify
- Dispose of unsuitable assets
- Develop an investment strategy suitable for the fund and the charity

- Special skills and expertise must be used
- Funds may be pooled for investment
- Delegation of authority to independent financial advisors permitted

IV. Expenditures from Endowment Funds

Historic Dollar Value

- Defined as amount contributed, not adjusted over time
- Old funds – no connection to purchasing power
- New funds – underwater (below hdv if value of gift declines)

UMIFA

- Permits spending appreciation above hdv, in prudence, after considering needs of the charity
- Probably permits spending “income” in addition

New Approach – no HDV and Better Guidance on Spending

- Subject to the gift instrument - donor intent
- “prudent for the uses, benefits, purposes, and duration for which the endowment fund is established”

Factors

- Duration and preservation of the fund
- Purposes of the institution and the fund
- General economic conditions
- Possible effect of inflation or deflation
- Expected total return
- Other resources
- Investment policy of the institution

Rule of Construction

“pay only the income” means UPMIFA rule applies: current expenditures and permanent duration

Drafting Committee Approach

- Prudence with guidance in statute provides sufficient direction
- Charities have not spent as much as they could have under UMIFA
- Charities have strong self-interest to protect endowments and to comply with donor intent
- Optional provisions should be provided so that states can consider alternatives

Optional Section #1 - Rebuttable Presumption of Imprudence

- Spending will be rebuttably presumed to be imprudent if spending in one year exceeds 7% of the asset value of the fund, computed over a rolling three-year period
- Not a safe harbor – no presumption of prudence for spending less than 7%

Arguments in favor

- Charities want guidelines
- Attorneys general want guidelines
- Needed to protect donor intent
- Could help to limit overspending
- Something similar in statutes in MA, NM, NH

Arguments against

- Could be viewed as a safe harbor and lead to overspending
- Could restrict prudent spending
- Will be out-of-date
- Does not provide for differences among charities

Optional Section #2 – Notification

- Charity must notify Attorney General if a spending authorization will take the charity's endowment funds, in the aggregate, below historic dollar value
- Only applies to a charity with total endowment funds of less than \$2,000,000

V. Modification or Termination of Restrictions

Equitable Deviation – focus on management and investment restrictions

- If restriction on management or investment becomes impracticable or wasteful or impairs the management or investment of the fund or
- If due to unanticipated circumstances modification will further purposes of fund

- Modify in accord with donor's probable intent
- Must notify Attorney General and obtain court approval

Cy Pres – focus on purpose or use restrictions

- If a purpose or use restriction becomes unlawful, impracticable, impossible, wasteful
- Modify consistent with purposes in gift instrument
- Must notify Attorney General and obtain court approval

Small, Old Fund

- Less than \$25,000
- More than 20 years
- Modify consistent with purposes in gift instrument
- Notify Attorney General and wait 60 days
- No court approval required

VI. Final Comments

Retroactive Application

- Charities need one set of rules, one set of books
- Rule of construction resolves an ambiguity – increases likelihood of giving effect to intent of donors

Default Statute

- Charities and donors can create their own rules

Finding UPMIFA

www.nccusl.org – link to Final Acts, select Management of Institutional Funds. This page has the final act, the act with comments, and information about legislative action in any jurisdictions in which the Act is introduced or enacted.

Questions or Comments:

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