

AMERICAN BAR ASSOCIATION  
NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS  
REPORT TO THE HOUSE OF DELEGATES

RECOMMENDATION

- 1 RESOLVED, That the American Bar Association approves the Uniform Prudent
- 2 Management of Institutional Funds Act, promulgated by the National Conference of
- 3 Commissioners on Uniform State Laws in 2006 as an appropriate Act for those states
- 4 desiring to adopt the specific substantive law suggested therein.



## REPORT

### UNIFORM PRUDENT MANAGEMENT OF INSTITUTIONAL FUNDS ACT

In 2006 the Uniform Law Commission promulgated the Uniform Prudent Management of Institutional Funds Act (UPMIFA) to replace the Uniform Management of Institutional Funds Act (UMIFA), promulgated originally in 1972. UMIFA was enacted in 47 states by 2006. It provided fundamental rules for the investment and expenditure of funds donated as “endowments” to charitable institutions. Those rules supported two general principles: 1) that assets would be invested prudently in diversified investments that sought growth as well as income; and, 2) that appreciation of assets could be prudently spent for the purposes of any endowment fund held by a charitable institution. These two principles are the twin lodestars of asset management for endowments since UMIFA virtually became the law of the land.

UPMIFA serves the twin lodestars as a needed upgrade of UMIFA. Both investment in assets and expenditure for charitable purposes have grown exponentially since the original UMIFA. There is a large amount of experience that needs to be recognized in the law. In addition, institutions and those that invest for them have learned a great deal about asset management, to the extent that UMIFA is now obsolete as a legal basis for making asset management decisions. So, in 2006, the Uniform Law Commission has promulgated UPMIFA to replace UMIFA.

#### INVESTMENT

UMIFA stated the first prudent investor rule in statutory law. It allowed investing in any kind of assets, pooling endowment funds for investment purposes, and delegating investment management to other persons (professional investment advisors), so long as the governing board of the charitable institution exercised ordinary business care and prudence in making these decisions. A range of factors guided the exercise of prudence. UMIFA was in its time a revolutionary advance over practices that relied on the limited investment opportunities available for managing trust assets, though endowments are not trusts.

UPMIFA provides a more exact set of rules for investing in a prudent manner, meaning better guidance for investment management than was the case under UMIFA. It requires investment “in good faith and with the care an ordinarily prudent person in a like position would exercise under similar purposes.” It requires prudence in incurring investment costs, “only costs that are appropriate and reasonable.” The guiding factors expand to include effect of inflation. It emphasizes that investment decisions with one

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fund must be made in relation with the overall resources of the institution and its charitable purposes. No investment decision may be made in isolation, but in light of the fund's entire portfolio, and as a part of an investment strategy "having risk and return objectives reasonably suited to the fund and to the institution."

There is an affirmative obligation to diversify assets unless "special circumstances" dictate otherwise. Assets must be reviewed as soon as they come into the possession of the institution in order to conform them to the investment strategy and objectives of the fund. Investment experts, whether in-house or hired for the purpose, are held to a standard of care consistent with that expertise.

UMIFA initiated an era of modern portfolio management for charitable institutions. UPMIFA provides all the standards and guidelines that subsequent experience tells us are the most appropriate for the purpose. Charitable institutions will have more precise standards to guide them. Courts will have more precise standards with which to measure prudence in the event of challenge. The result will be better management of assets and more money for programs supported by endowments.

## **EXPENDITURE**

UMIFA also initiated the concept of total return expenditure of endowment assets for charitable program purposes. It expressly allows prudent expenditure of appreciation. This means that asset growth and income may be appropriated for program purposes. The only limitation upon the institution was a kind of floor for expenditure. A fund could not be spent below "historic dollar value." The idea of investment for total return and then the expenditure of funds by a measure of total return including appreciation and income, were really initiated in UMIFA.

UPMIFA, of course, does not reverse the original rule on appreciation, except that it no longer provides the floor of "historic dollar value." Express new rules of prudence replace the old general rule and make the need for a floor unnecessary. UPMIFA states that the institution "may appropriate for expenditure or accumulate so much of an endowment fund as the institution determines to be prudent for the uses, benefits, purposes and duration for which the endowment fund is established." This is not radically different from UMIFA, but prudence is articulated more finely in seven criteria that guide the institution in its yearly expenditure decisions: "1) duration and preservation of the endowment fund; 2) the purposes of the institution and the endowment fund; 3) general economic conditions; 4) effect of inflation or deflation; 5) the expected total return from income and the appreciation of investments; 6) other resources of the institution; and, 7) the investment policy of the institution." UMIFA does not have standards of this kind to guide the institution in making expenditure decisions. These standards are not greatly different from the standards that apply to

investment decision-making, thus unifying both investment and expenditure decisions more concretely.

UPMIFA has an optional provision that allows states to enact another kind of safeguard for expenditure. States may or may not want to rely upon the basic rule of prudence, but if they do not want to rely upon it solely, UPMIFA provides that a rebuttable presumption of imprudence arises if the institution expends an amount greater than seven percent of fair market value as calculated in an averaging formula over the prior three years. The standards of prudence should be sufficient to restrain expenditure decisions. The standards that guide charitable institutions for total return expenditure under current practices fall well below this seven percent guideline. Five percent is considered high as a decision of prudence. The standards articulated in UPMIFA will automatically call decisions that exceed these currently accepted limits into question as a matter of prudence. So the seven percent rule is likely not to be necessary. It is in UPMIFA for those states uncomfortable with the general standards.

## **OTHER IMPROVEMENTS**

UPMIFA applies to all funds held by charitable institutions. UMIFA applied only to endowments. UPMIFA recognizes and protects donor intent more broadly than UMIFA did. The release of donor restrictions on funds is more comprehensively addressed in UPMIFA than in UMIFA. A donor may consent to release or modify restrictions in a record. A court may consider release or modification when a restriction has become wasteful or impracticable, and impairs management of a fund because of circumstances not anticipated by a donor, upon petition of the institution. A court may apply broader principles of release or modification (exercise of cy pres) than is the case under UMIFA. In addition, UPMIFA requires notification of a state's attorney general, who has the usual obligation of oversight for charities, if a procedure in court to release or modify restrictions is initiated by an institution. In addition, UPMIFA has a provision for modifying or releasing restrictions of very small (less than \$25,000.00 suggested) and very old (over 20 years suggested) institutional funds for which the restricted purposes clearly cannot be satisfied and new purposes consistent with the original endowment can be established without resort to a judicial proceeding. Again, notice to a state's chief charitable regulator is required.

## **CONCLUSION**

UPMIFA does not radically change institutional investment or expenditure practices. It brings them up-to-date over the original UMIFA, following more than 30 years of good experience. The better charitable institutions manage investments and prudently control expenditures, the more money they have for program purposes. It is prudent, therefore, for the states to enact UPMIFA as soon as practicable.

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The work of the Drafting Committee is available at [www.nccusl.org](http://www.nccusl.org), the website of the Conference.

Respectfully submitted,

Howard J. Swibel  
President

NATIONAL CONFERENCE OF  
COMMISSIONERS ON UNIFORM

STATE LAWS

February 2007

**GENERAL INFORMATION FORM**

To Be Appended to Reports with Recommendations  
(Please refer to instructions for completing this form.)

Submitting Entity: National Conference of Commissioners on Uniform State Laws

Submitted by: John M. McCabe, Legal Counsel

1. Summary of Recommendation(s).

The National Conference of Commissioners on Uniform State Laws requests approval of the Uniform Prudent Management of Institutional Funds, by the ABA House of Delegates. The Uniform Prudent Management of Institutional Funds Act has been approved by the National Conference in 2006.

2. Approval by Submitting Entity.

The National Conference of Commissioners on Uniform State Laws approved it in July, 2006.

3. Has this or a similar recommendation been submitted to the House or Board previously?

Yes. This Act supersedes the Uniform Management of Institutional Funds Act approved by the ABA in 1973.

4. What existing Association policies are relevant to this recommendation and how would they be affected by its adoption?

None known, But the Association has approved the earlier act the new Uniform Act supersedes.

5. What urgency exists which requires action at this meeting of the House?

After a Uniform Act is approved by the National Conference, Commissioners work for adoption of the proposal by the States. Legislatures are urged to adopt Uniform Acts exactly as written, to "promote uniformity in law among the several States." Approval of the Uniform Prudent Management of Institutional Funds Act at the Mid-Year Meeting in February 2007 is desired to encourage swift enactment of the Uniform Act in the state legislatures.

6. Status of Legislation. (If applicable.)

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None.

7. Cost to the Association. (Both direct and indirect costs.)

Not applicable.

8. Disclosure of Interest. (If applicable.)

None.

9. Referrals.

Pursuant to the agreement between the NCCUSL and the ABA, all members of the House of Delegates and Chairs of all ABA entities were advised of the drafting project and those that expressed interest were provided with tentative drafts, as well as the final Act and Report. The work of the Drafting Committee is available at [www.nccusl.org](http://www.nccusl.org), the website of the Conference.

The ABA Advisor was Carol G. Kroch.

10. Contact Person. (Prior to the meeting.)

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11. Contact Person. (Who will present the report to the House.)

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12. Contact Persons Regarding Amendments to This Recommendation.

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## EXECUTIVE SUMMARY

1. Summary of the Recommendation.

That the ABA approves the Uniform Prudent Management of Institutional Funds as an appropriate “Act for those States desiring to adopt the substantive law suggested therein.”

2. Summary of the issue which the recommendation addresses.

The Uniform Prudent Management of Institutional Funds Act provides rules governing the investment and expenditure of funds held by charitable institutions. It proposes prudent management rules for both investment and expenditure and up-grades the procedures for changing antiquated and unworkable restrictions on such funds. It replaces the Uniform Management of Institutional Funds Act originally promulgated by the uniform law commissioners in 1972.

3. Please explain how the proposed policy position will address the issue.

The Uniform Act provides appropriate rules for the objective as stated in 2. above.

4. Summary of any minority views or opposition which have been identified.

The NCCUSL is not aware of any minority views or opposition to the Uniform Act.