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UPMIFA: Uniform Prudent Management Of Institutional Funds Act

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California law governing the management, investment and spending of donor–created endowment funds held by charitable organizations has recently changed. Until January 1, 2009, endowment funds were regulated by the Uniform Management of Institutional Funds Act ("UMIFA"), but endowment funds established after January 1, 2009 (the "Effective Date") will be regulated by the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"). Endowment funds that were established prior to the Effective Date are subject to UPMIFA only with respect to actions taken after the Effective Date. Thus, effectively, UPMIFA applies to all donor–created endowment funds held by charitable institutions in California.

UPMIFA was enacted to update the prudence standard and to provide flexibility in the management of endowment funds in market downturns and when modifying restrictions on endowment funds due to changed circumstances. This newsletter provides a comparison between the major provisions of UMIFA and UPMIFA.

WHAT IS AN ENDOWMENT FUND UNDER UPMIFA?

UPMIFA defines an *endowment fund* as a fund that is established or created by a donor that is not wholly expendable by the institution on a current basis under the terms of the gift instrument. Specifically excluded from UPMIFA are endowments created by the charitable institution itself and program–related assets.

UPMIFA defines a *gift instrument* as any record or records from a donor. A *record* is defined as information that is written on a tangible medium or stored electronically (including email). It includes an institutional solicitation or governance documents, such as bylaws. A record is part of the gift instrument so long as the donor and the charity were, or should have been, aware of its terms.

STANDARD OF CARE

Under UMIFA, when investing for the benefit of an institution, the members of the governing board of the charitable institution (the "Board") had to exercise ordinary business care and prudence. While administering the endowment fund pursuant to the prudent person standard, individual investments were considered as part of the overall investment strategy. UMIFA provided the Board with a range of factors to be used as a guide for investment decisions in order to meet the prudent person standard of care.

UPMIFA expands upon UMIFA and provides a more precise set of rules for investing in a prudent manner. The Board must exercise the care of the ordinary prudent person. The charity may invest in any kind of property as long as it is consistent with the standard of care, and may only incur reasonable costs when managing and investing the endowment fund. The factors the Board must consider in investing include the general economic conditions, the effects of inflation or deflation, tax consequences, the role of each investment within the overall portfolio, the expected total return from income and appreciation, the other resources of the institution, the needs of the institution, and the special relationship of the asset to the institution, if any. Individual asset decisions must be made in the context of the total portfolio, and the Board has a duty to diversify and rebalance a fund, as necessary.

UPMIFA allows a charity to delegate the management and investment decisions to committees, officers, employees or external managers. The charity must act prudently in selecting agents, establishing the scope of the work delegated, and reviewing the performance of the agent.

SPENDING FROM THE ENDOWMENT FUND

UMIFA provided that a charity could spend all of the income (e.g., interest and dividends) and appreciation as long as the endowment fund was not spent below the historic dollar value. Simply put, *historic dollar value* was defined as the aggregate fair value of each gift on the date each was donated to the fund. Historic dollar value acted as a floor below which any given fund could not be spent.

UPMIFA eliminates the concept of historic dollar value and allows a charity to expend "so much as the institution determines is prudent for the uses, benefits, purposes and duration for which the endowment fund is established."; There are various factors that the Board may consider when making expenditure decisions. These factors included the duration and preservation of the fund, the purposes of the institution and the fund, the general economic conditions, the possible effect of inflation or deflation, the expected total return from income or appreciation, other resources of the institution and the investment policy of the institution. The gift instrument cannot vary the foregoing except under very narrow circumstances.

In order to safeguard an endowment fund against excessive spending, UPMIFA includes a provision which states that spending greater than 7 percent of the fair market value of an endowment fund (averaged over a three–year period) creates a rebuttable presumption of imprudence. However, spending less than the seven percent does not create a presumption of prudence. It should be noted that this 7 percent presumption does not apply to postsecondary educational institutions, presumably to encourage them to spend from their endowments.

REVISING OR RELEASING PURPOSE RESTRICTIONS

In order to release a restriction on an endowment fund under UMIFA, the written consent of the donor was required. If the donor was deceased, then a court ruling would be needed with notice given to the Attorney General. The standard that would be used to determine whether a release was appropriate was whether the restriction had become "obsolete or impractical."

UPMIFA provides a more thorough treatment regarding the modification of restrictions on endowment funds than UMIFA. As long as the donor is able to do so, he or she may consent to a revision or release of a charitable purpose or management restriction. In the event that the donor is deceased or incapacitated, a charity may petition the probate court requesting the release of a management restriction or charitable purpose that has become impracticable, wasteful (a new criterion), unlawful or impossible to achieve. In addition to petitioning the court, the charity must notify the Attorney General of its request.

UPMIFA contains a provision that provides a charitable institution with the ability to modify a restriction on a fund without a court order and without donor consent under certain circumstances. The provision applies to endowment funds with a fair market value of less than $100,000 that are over 20 years old. If it is determined by the charitable institution that a restriction on the fund is unlawful, impracticable, impossible to achieve or wasteful, then the charity can provide a 60–day notice to the Attorney General requesting a modification. If the Attorney General approves the request, the charitable institution may modify the restriction so long as the modification is as consistent as possible with the donor's original charitable purpose, as expressed in the documents that were part of the original gift.

CONCLUSION

UPMIFA brings the laws regulating the management, investment and spending of endowment funds in line with the current investment environment, and provides greater flexibility for charitable institutions. The change in the law provides greater guidance for those delegated with duties related to the management of endowment funds.

back to top

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