

Dear Prudence, Meet The Brand New Day<sup>1</sup>

# Michigan's New Uniform Prudent Management Of Institutional Funds Act

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## Introduction

Endowment funds are suffering. With average declines in fund value of roughly 20 percent during the past year, many Michigan nonprofits are struggling to properly manage and invest “underwater” endowment funds that have plunged below the historic value of the original gifts with which the funds were created. Michigan law has made facing those challenges more difficult. Help is on way.

In 1972, the National Conference of Commissioners on Uniform State Laws (“NCCUSL”) approved the Uniform Management of Institutional Funds Act (“UMIFA”). UMIFA regulated the investment and expenditure of funds held by charitable institutions. Forty-seven states enacted versions of UMIFA, including Michigan, which enacted its version (“MI-UMIFA”) in 1976.<sup>2</sup>

Portions of UMIFA have become outdated, including the prudence standards for management and investment, the rules governing expenditures from endowment funds, and the provisions regarding the release and modification of restrictions on charitable funds. In response to the need for modernization, NCCUSL promulgated the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) to replace UMIFA.

## Promulgation and Enactment of UPMIFA

### *Promulgation by NCCUSL*

### History

The approval of the final version of UPMIFA was years in the making. NCCUSL created a committee (“Drafting Committee”) in the autumn of 2000 to review UMIFA and determine whether a revision was needed. Drafting Committee began work in 2002. At its annual meeting in July 2006, NCCUSL approved the final version of UPMIFA and recommended it for enactment by the states.<sup>3</sup>

### Purposes

A driving force behind the development of UPMIFA was the need to update the rules applicable to charitable funds to reflect changes in investment and expenditure strategies over the past thirty-five years. A major goal of UPMIFA is the application of consistent standards for the management and investment of charitable funds so that the same standards apply regardless of whether a charitable organization is organized

as a trust, a nonprofit corporation, or another type of entity.<sup>4</sup> In order to achieve consistency among the uniform laws, UPMIFA derives portions of its provisions from the Uniform Prudent Investor Act (“UPIA”)<sup>5</sup> and the Uniform Trust Code (“UTC”).<sup>6</sup> Specifically, UPMIFA adopts a modern prudence standard based on UPIA, modernizes the rules governing expenditures in order to provide more guidance and flexibility to institutions, and updates the provisions related to the release and modification of fund restrictions based on similar provisions in the UTC.<sup>7</sup>

### State Enactments

Since its approval in July 2006, 33 states have enacted versions of UPMIFA. UPMIFA bills have been introduced in 11 other states, including Michigan.<sup>8</sup>

### *Michigan Legislation*

### Legislative History

Michigan's version of UPMIFA (“MI-UPMIFA”) was introduced in the state Senate and passed unanimously on April 22, 2009.<sup>9</sup> It is now being considered in the House by its Banking and Financial Services Committee. Enactment is expected in 2009. An effective date has yet to be determined, although there is good reason to give it immediate effect, as was done with Michigan's enactment of UMIFA in 1976.

### Purposes

In summary, replacement of Michigan's UMIFA with MI UPMIFA will accomplish the following:

- Require an institution managing and investing an institutional fund to consider the institution's charitable purposes and the purposes of the fund.
- Establish a good faith and prudent person standard for each person responsible for managing and investing an institutional fund.
- Specify factors that would have to be considered, and rules that would apply, in the management and investment of an institutional fund.
- Allow an institution to appropriate for expenditure or accumulate amounts of an endowment fund that were prudent for its uses, benefits, purposes, and duration.
- Require an institution to consider specific factors in determining to appropriate or accumulate amounts in an endowment fund.

- Specify circumstances under which an institution could delegate the management and investment of an institutional fund to an agent.
- Specify conditions under which an institution could release or modify a restriction contained in a gift instrument on the management, investment, or purpose of an institutional fund.
- Require the Michigan Attorney General to be notified and given an opportunity to be heard on the matter of releasing or modifying a restriction in a gift instrument.<sup>10</sup>

## Key Definitions in MI-UPMIFA

### *Institution*

- A person, other than an individual, organized and operated exclusively for charitable purposes. The exclusion of “individual” is not intended to exclude a corporation sole.
- A government or governmental subdivision, agency, or instrumentality, to the extent that it holds funds exclusively for a charitable purpose.
- A trust that has charitable interests, but only after all non-charitable interests have terminated. This definition excludes, for example, charitable remainder trusts that have at least one individual as a current trust beneficiary.<sup>11</sup>

### *Institutional Fund*

A fund held by an institution exclusively for charitable purposes, whether the fund is currently expendable or subject to restrictions. The term does not include:

- Program-related assets that an institution holds primarily to conduct its charitable purposes rather than for investment purposes, for example, land adjacent to its campus that a university holds for future development.
- A fund held for an institution by a trustee that is not an institution, unless the fund is held by the trustee as a component trust or fund of a community foundation.<sup>12</sup> The effect is to exclude charitable trusts managed by individuals and almost all charitable trusts managed for financial institutions.
- A fund in which a beneficiary that is not an institution has an interest, other than an interest that could arise upon violation or failure of the purposes of the fund.<sup>13</sup>

### *Gift Instrument*

A written record or records, including an institutional solicitation, under which property is granted to, transferred to, or held by an institution as an institutional fund.<sup>14</sup> A record will only become a gift instrument if both the donor and the institution were or should have been aware of its terms when the

donor made the gift. Solicitation material may constitute a gift instrument. For example, a written solicitation suggesting that any gift received pursuant to the solicitation will be held as endowment may be integrated with other writings and may be considered part of the gift instrument.<sup>15</sup>

### *Endowment Fund*

An institutional fund or part thereof that, under the terms of a gift instrument, is not wholly expendable by the institution on a current basis. The term does not include assets that an institution designates as an endowment fund for its own use such “board-designated” funds that are institutional funds but not endowment funds.<sup>16</sup>

## Comparison of Key UMIFA and UPMIFA Provisions

### *Applicability*

Although MI-UPMIFA applies to institutional funds existing on or established on or after the effective date, for institutional funds existing on the effective date MI-UPMIFA applies only to actions and decisions occurring on or after the effective date.<sup>17</sup>

### *Standard of Conduct for the Management and Investment of Institutional Funds*

#### MI-UMIFA Provisions

MI-UMIFA required that in managing, spending, and investing endowment funds, the persons responsible for a fund must “exercise ordinary business care and prudence under the facts and circumstances prevailing at the time of the action or decision.”<sup>18</sup> In addition, the persons responsible for a fund had to consider the following factors in exercising their duties:

- the long-term and short-term needs of the institution in carrying out its educational, religious, or charitable purposes;
- the present and anticipated financial requirements of the institution;
- the expected return on investments;
- price level trends; and
- general economic conditions.<sup>19</sup>

MI-UMIFA authorized an institution to retain property contributed by a donor in the hope of obtaining additional future contributions.<sup>20</sup>

#### MI-UPMIFA Provisions

MI-UPMIFA requires that an institution consider the charitable purposes of the institution and the purposes of the fund when managing and investing an institutional fund. This requirement and all other duties imposed under MI-UPMIFA are subject to the intent of a donor as expressed in the gift instrument.<sup>21</sup> In addition to these overarching standards,

A driving force behind the development of UPMIFA was the need to update the rules applicable to charitable funds to reflect changes in investment and expenditures strategies over the past thirty-five years.

MI-UPMIFA outlines the following duties for institutions and those responsible for the management and investment of institutional funds:

#### *Duty of Care*

A person responsible for managing and investing an institutional fund must “manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.”<sup>22</sup> A person with special skills or expertise must use those skills or that expertise in managing and investing institutional funds.

An institution must also consider the following factors in making management and investment decisions for institutional funds:

- general economic conditions;
- the possible effect of inflation or deflation;
- the expected tax consequences, if any, of investment decisions or strategies;
- the role that each investment or course of action plays within the overall investment portfolio of the fund;
- the expected total return from income and the appreciation of investments;
- other resources of the institution;
- the needs of the institution and the fund to make distributions and to preserve capital; and
- an asset’s special relationship or special value, if any, to the charitable purposes of the institution.<sup>24</sup>

#### *Duty of Loyalty*

MI-UPMIFA notes that those managing and investing institutional funds are subject to the duty of loyalty imposed by other laws.<sup>25</sup> Thus, the duty of loyalty under nonprofit corporation law will apply to institutions organized as nonprofit corporations, and the trust law duty of loyalty will apply to charitable trusts.

#### *Duty to Manage Costs and Verify Facts*

An institution may incur only costs that are reasonable in relation to the fund assets, the purposes of the institution, and the skills available to the institution.<sup>26</sup> Those responsible for managing an institutional fund must also make a reasonable effort to verify facts relevant to the management and investment of the fund.<sup>27</sup>

#### *Duty to Diversify*

Under MI-UPMIFA, an institution must diversify the investments of an institutional fund unless special circumstances exist in which the purposes of the fund are better served without diversification.<sup>28</sup> Within a reasonable time after receiving property, an institution must decide whether to retain or dispose of the property in order to balance out the portfolio and maintain compliance with the purposes of the institution.<sup>29</sup> An institution may not retain an asset solely based on the hope of obtaining future contributions from the same donor. The possibility of receiving future contributions is only one factor to be considered in the overall decision. Decisions about a particular asset must be made in the context of

the investment portfolio as a whole and as part of an overall investment strategy.<sup>30</sup>

### **Reasons for the Change**

Although MI-UMIFA contains a general standard of “ordinary business care and prudence,” many institutions desired additional guidance and clarity with respect to the standard of prudence and other standards of conduct applicable to the management and investment of institutional funds.<sup>31</sup> MI-UPMIFA offers specific guidance by stipulating several duties and enumerating factors that must be considered in managing and investing an institutional fund. The prudence standard under MI-UPMIFA is derived from and is consistent with the standard under UPIA and thus helps achieve the goal of a common standard of prudence for all types of charitable institutions.<sup>32</sup>

#### *Expenditure of Endowment Funds*

##### **MI-UMIFA Provisions**

The rules regarding expenditures from endowment funds under MI-UMIFA were based on the concept of “historic dollar value.” Historic dollar value is the aggregate fair market value of an endowment fund at the time it became an endowment fund, each subsequent donation to the fund at the time the donation is made, and each accumulation made pursuant to a direction in the gift instrument at the time the accumulation is added to the fund.<sup>33</sup> Under MI-UMIFA, the persons responsible for a fund could appropriate for expenditure only the net appreciation, realized and unrealized, in the fair market value of endowment fund assets over the historic dollar value of the fund to the extent such appropriation was prudent.<sup>34</sup>

##### **MI-UPMIFA Provisions**

Under MI-UPMIFA, the assets in an endowment fund are donor-restricted until appropriated for expenditure by the institution.<sup>35</sup> MI-UPMIFA eliminates the concept of historic dollar value. Instead, an institution may appropriate for expenditure or accumulate so much of an endowment fund as the institution deems prudent for the uses, benefits, purposes, and duration for which the endowment fund is established.<sup>36</sup> In determining whether to appropriate or accumulate fund assets, the institution must act in good faith with the care that an ordinarily prudent person in a like position would exercise under similar circumstances. MI-UPMIFA also lists the following factors that must be considered in the determination to spend or accumulate endowment fund assets:

- the duration and preservation of the endowment fund;
- the purposes of the institution and the endowment fund;
- general economic conditions;
- the possible effect of inflation or deflation;
- the expected total return from income and the appreciation of investments;
- other resources of the institution; and
- the investment policy of the institution.<sup>37</sup>

Pooling of funds is permitted, but the pooled funds will be considered individually for purposes of the rules relating to spending.<sup>38</sup>

MI-UPMIFA contains a rule of construction that terms in a gift instrument designating a gift as an endowment, or a direction or authorization in the gift instrument to use only “income,” “interest,” “dividends,” or “rents, issues, or profits,” or “to preserve principal intact” have the effect of creating a permanent endowment fund but do not otherwise limit the authority to appropriate for expenditure or accumulate.<sup>39</sup>

### Reasons for the Change

The Drafting Committee concluded that UMIFA’s endowment spending rule created numerous problems and that restructuring the rule would benefit charities, their donors, and the public. The problems include:

- Historic dollar value fixes valuation at a moment in time, and that moment is arbitrary. The determination of historic dollar value can vary significantly depending upon when in the market cycle the donor dies.
- After a fund has been in existence for a number of years, historic dollar value may become meaningless. Assuming reasonable long term investment success, the value of the typical fund will be well above historic dollar value, and historic dollar value will no longer represent the purchasing power of the original gift. Without better guidance on spending the increase in value of the fund, historic dollar value does not provide adequate protection for the fund. If a charity views the restriction on spending simply as a direction to preserve historic dollar value, the charity may spend more than it should.
- UMIFA does not provide clear answers to questions a charity faces when the value of an endowment fund drops below historic dollar value. A fund that is so encumbered is commonly called an “underwater” fund. Conflicting advice regarding whether an organization could spend from an underwater fund has led to difficulties for those managing charities. If a charity concluded that it could continue to spend trust accounting “income” until a fund regained its historic dollar value, the charity might invest for current yield rather than on a total-return basis. Thus, the historic dollar value rule can cause inappropriate distortions in investment policy and can ultimately lead to a decline in a fund’s real value. If, instead, a charity with an underwater fund continues to invest for total return consistent with the charity’s tolerance for risk, the charity may be unable to spend anything from an underwater endowment fund for several years. Yet, the inability of a charity to spend anything from an endowment may be contrary to donor intent.<sup>40</sup>

The Drafting Committee concluded that providing clearly articulated guidance on the prudence rule for spending from an

endowment fund, with emphasis on the permanent nature of the fund, would provide the best protection of the purchasing power of endowment funds.<sup>41</sup>

MI-UPMIFA eliminates the concept of historic dollar value and shifts the focus to preservation of the real value of an endowment fund. MI-UPMIFA emphasizes the purposes of a particular endowment fund, as opposed to the general purposes of the institution, and encourages consideration of the total assets of an endowment fund. MI-UPMIFA guides institutions with a more comprehensive prudence standard for expenditures so that the benchmark of historic dollar value is no longer necessary.<sup>42</sup>

### Distinguishing Legal and Accounting Standards

During the drafting of UPMIFA, concern arose regarding inconsistencies between the legal restrictions imposed on endowment fund expenditures under UPMIFA and the accounting standards used for reporting endowment fund assets on financial statements. Paragraph 22 of Statement of Financial Accounting Standards No. 117 (“FAS 117”), adopted by the Financial Accounting Standards Board (“FASB”) in 1993, provides as follows:

A statement of activities shall report gains and losses recognized on investments and other assets (or liabilities) as increases or decreases in unrestricted net assets unless their use is temporarily or permanently restricted by explicit donor stipulations or by law. For example, net gains on investment assets, to the extent recognized in financial statements, are reported as

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increases in unrestricted net assets unless their use is restricted to a specified purpose or future period. If the governing board determines that the relevant law requires the organization to retain permanently some portion of gains on investment assets of endowment funds, that amount shall be reported as an increase in permanently restricted net assets.<sup>43</sup>

The Basis for Conclusions section of FAS 117 elaborates on this position and provides:

The Board agreed and concluded that there is no need to delay recognizing available net gains [on endowment fund investments] in unrestricted or temporarily restricted net assets until such time as the organization’s governing board acts to appropriate them for use. Decisions about when to spend resources generally do not bear on the issue, which is whether the resources are available for spending . . . [r]estricted net assets result only from a donor’s stipulation that limits the organization’s use of net assets or from a law that extends the donor’s stipulation to enhancements (including holding gains) and diminishments of those net assets.<sup>44</sup>

The Basis For Conclusions section of FAS 117 also explains FASB’s position that the determination of whether donor

stipulations or relevant law impose restrictions on the use of net appreciation depends on the facts and circumstances of each case.<sup>45</sup>

FASB's positions changed in response to UPMIFA. On August 6, 2008, FASB issued FASB Staff Position FAS 117-1 ("FSP 117-1"), entitled "Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for All Endowment Funds."<sup>46</sup> FSP 117-1 addresses net asset classification in light of UPMIFA's elimination of historic dollar value and the shift in focus to expenditures from an endowment fund as a whole, rather than only the net appreciation.<sup>47</sup>

Nonprofits that are subject to UPMIFA must classify the portion of the donor-restricted endowment fund that is perpetual in duration as permanently restricted net assets. The amount classified as permanently restricted is the amount that must be retained permanently in accordance with explicit donor restrictions, or if such restrictions are absent, the amount the organization's governing board determines must be retained permanently consistent with relevant law. Accordingly, permanently restricted net assets may, in certain circumstances, include accumulated earnings on those assets.

MI-UPMIFA provides that "unless stated otherwise in the gift instrument, the assets in the endowment fund are donor-restricted assets until appropriated for expenditure by the institution."<sup>48</sup> This differs from previous guidance under FASB 124 that considered earnings on donor-restricted endowments to be unrestricted (whether or not appropriated for expenditure by the organization) unless otherwise restricted by donors or by specific relevant law.

As a result of this change, the portion of donor-restricted endowment funds that is not classified as permanently restricted net assets must now be classified as temporarily restricted net assets (time restricted) until appropriated for expenditure by the organization. FAS 117-1 states that an appropriation for expenditure occurs upon approval for expenditure. Nonprofits affected by this change must restate their financial statements by reclassifying certain amounts previously reported as unrestricted to temporarily restricted net assets to the extent they have not already been appropriated for expenditure.

Regardless of the treatment of an endowment fund for accounting purposes, the comments to UPMIFA emphasize that an endowment fund is not considered unrestricted from a legal standpoint.

#### **Additional Financial Disclosures**

All nonprofits with board-designated or donor-restricted endowment funds, whether or not subject to an enacted version of UPMIFA, must make additional disclosures in their financial statements under FAS 117-1.<sup>50</sup> These additional disclosures include:

- The governing board's interpretation of the law(s) underlying the net asset classification of the donor-restricted endowment funds;

- The organization's policy for appropriation of endowment assets for expenditure;
- The organization's endowment investment policies, including a description of the organization's return objectives and risk parameters, how those objectives relate to the organization's endowment spending policy, and the strategies employed for achieving those objectives;
- The composition of the organization's endowment by net asset class at the end of the period, in total, and by type of endowment fund, showing donor-restricted endowment funds separately from board-designated endowment funds; and,
- A reconciliation of the beginning and ending balance of the organization's endowment, in total and by net asset class, including, at minimum, the following line items (as applicable): investment return separated into investment income (for example, interest, dividends and rents) and net appreciation or depreciation of investments, contributions, amounts appropriated for expenditure, reclassifications, and other changes.

#### *No Rebuttable Presumption of Imprudence*

UPMIFA includes an optional provision that creates a rebuttable presumption of imprudence if more than seven percent of the fair market value of an endowment fund is appropriated for expenditure in a given year.<sup>51</sup> MI-UPMIFA does not include this provision. Evidence reviewed by the Drafting Committee suggests that at present few funds can sustain spending at a rate above five percent.<sup>52</sup> Further, spending at a lower rate, particularly in the early years of an endowment, may result in greater distributions over time.<sup>53</sup>

There are drawbacks to the rebuttable presumption of imprudence. First, as with the concept of historic dollar value, some institutions may misconstrue the meaning of the percentage as being a safe harbor for prudent conduct, even though UPMIFA expressly provides that there is no presumption of prudence for expenditures that are less than the relevant threshold percentage.<sup>54</sup> Also, an institution might spend less than the percentage limit each year but still be imprudently spending too much of a fund's value. In addition, a single fixed percentage is unlikely to be appropriate for a multitude of diverse institutions, and the percentage does not adjust to reflect changing economic conditions.<sup>55</sup>

#### *Delegation of Management and Investment*

##### **MI-UMIFA Provisions**

MI-UMIFA authorized the governing board to delegate their investment authority to committees, officers, or employees of the institution or fund, or to other agents, and to contract with independent investment advisors for investment and management services.<sup>56</sup> The persons responsible for delegating management and investment decisions were subject to the general MI-UMIFA standard of conduct of ordinary business care and prudence.<sup>57</sup>

**MI-UPMIFA Provisions**

MI-UPMIFA also authorizes the delegation of management and investment decisions to external agents to the extent that such delegation is prudent under the circumstances.<sup>58</sup> MI-UPMIFA provides guidance with respect to the standards applicable to institutions and agents when management and investment authority is delegated. An institution must act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances, in: (a) selecting an agent; (b) establishing the scope and terms of the delegation, consistent with the purposes of the institution and the institutional fund; and (c) periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the scope and terms of the delegation.<sup>59</sup> If an institution complies with the standard set forth above, the institution will not be liable for an agent's decisions or actions.<sup>60</sup>

An agent who accepts the delegation of management or investment authority owes a duty to the institution to exercise reasonable care in carrying out the scope and terms of the delegation.<sup>61</sup> An agent accepting delegation of a management or investment function under MI-UPMIFA is subject to the personal jurisdiction of Michigan courts in all proceedings arising from or related to the delegation or to the performance of the delegated function.<sup>62</sup>

MI-UPMIFA Section 5 does not address the issues of internal delegation and potential liability for internal delegation and does not affect Michigan laws that govern personal liability of directors or trustees for matters outside the scope of Section 5. Directors must look to nonprofit corporation law for these rules, while trustees will look to trust law.<sup>63</sup>

**Reasons for the Change**

The delegation provision is optional under UPMIFA, because the Drafting Committee found that many states already provide sufficient authority to delegate through other statutes such as nonprofit corporation statutes and state enactments of UPIA.<sup>64</sup> Because this is not the case in Michigan, the delegation provisions are included in MI-UPMIFA and offer more detailed guidance for institutions and their agents than the comparable MI-UMIFA provisions.

*Modification and Release of Restrictions*

**MI-UMIFA Provisions**

MI-UMIFA allowed a restriction imposed on the use or investment of an institutional fund by a gift instrument to be released with the written consent of the donor.<sup>65</sup> In addition, if a donor was unavailable, an institution could apply to a court having jurisdiction for the release of a restriction that

was obsolete, inappropriate, or impracticable.<sup>66</sup> These provisions permitted only the release of existing restrictions, not a modification.

**MI-UPMIFA Provisions**

*Donor Consent to Release or Modify*

Under MI-UPMIFA, an institution may release or modify a restriction if the donor consents in writing, provided that the fund continues to be used for a charitable purpose.<sup>67</sup>

*Court Approval of Equitable Deviation*

An institution may apply to a court for the modification of a restriction regarding the management or investment of an institutional fund if any of the following are true:

- the restriction has become impracticable or wasteful;
- the restriction impairs the management or investment of the fund; or
- modification will further the purposes of the fund due to circumstances not anticipated by the donor.

To the extent practicable, any modification must be made in accordance with the donor's probable intention.<sup>68</sup>

*Court Application of Cy Pres*

A court may also modify the purpose of a fund or a restriction on the use of a fund if the purpose or restriction has become unlawful, impracticable, impossible to achieve, or wasteful.<sup>69</sup>

*Modification of Small Old Funds*

An institution may release or modify a restriction without donor or court consent if the restriction is unlawful, impracticable, impossible to achieve, or wasteful, and if all of the following conditions are satisfied:

- the restricted fund has a total value of less than \$25,000;
- more than 20 years have passed since the establishment of the fund; and
- the institution uses the property in a manner that is consistent with the charitable purposes expressed in the gift instrument.<sup>70</sup>

Release or modification of restrictions by a court or with respect to a small old fund requires that the Michigan Department of Attorney General be notified.<sup>71</sup> The Drafting Committee decided not to require that notification be given to the donor.<sup>72</sup> This leaves open the question of whether and under what circumstance a donor may have standing to object.

**Reasons for the Change**

MI-UPMIFA updates the rules on modification and release of restrictions in order to provide for better protection of donor intent and for more efficient administration of endowment funds. The new statute is consistent with the

MI-UPMIFA also authorizes the delegation of management and investment decisions to external agents to the extent that such delegation is prudent under the circumstances.

doctrines of equitable deviation and cy pres under the UTC.<sup>73</sup> MI-UPMIFA clarifies and supplements MI-UMIFA by allowing an institution to ask a court for the modification of a restriction or a fund purpose rather than a full release of such restriction or purpose. This protects donor intent by ensuring that a restriction or purpose will be modified and left in place to the extent possible rather than being completely released.<sup>74</sup>

MI-UPMIFA also encourages efficiency by enabling institutions to modify small funds that are more than twenty years old. Because the cost of requesting a court to modify a small fund would likely be disproportionate to the value of the fund, this provision offers a useful alternative for an institution wishing to modify such a fund for more efficient administration.<sup>75</sup>

Under a non-UPMIFA addition addressing community foundation concerns, MI-UMIFA provides that it does not affect the right of a governing body of an institution to exercise the power to modify restrictions contained in a gift instrument if such a right is conferred under the institution's governing instruments or under the gift instrument itself.<sup>76</sup>

## Conclusion

MI-UPMIFA promises welcome relief and guidance for endowment fund managers in Michigan. The new act updates the rules governing institutional endowment funds in order to provide better guidance to institutions and the persons responsible for managing, investing, and spending the funds. Enactment also brings the rules governing charitable endowment funds closer to other statutes applicable to charitable organizations in order to achieve consistent treatment of institutional funds without regard to the form of organization.

Hey, let's be careful out there.<sup>77</sup>

## Endnotes

1. Lyric by J. Lennon (1968). "Dear Prudence" was written about actress Mia Farrow's sister Prudence, who was present when The Beatles visited Maharishi Mahesh Yogi in India. Prudence, focused on meditation, stayed in her room for the majority of their stay. Hence, the lyric inviting her to come out and play and to meet the brand new day.

2. MICHIGAN UNIF. MGMT. OF INSTITUTIONAL FUNDS ACT (effective June 17, 1976) MCL §§ 451.1201-.1210.

3. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT (2006) with prefatory note and commentary (36 pages) may be viewed at [www.law.upenn.edu/bll/archives/ulc/umoifa/2006final\\_act.pdf](http://www.law.upenn.edu/bll/archives/ulc/umoifa/2006final_act.pdf).

4. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT, prefatory note (2006).

5. UNIF. PRUDENT INVESTOR ACT (1994).

6. UNIF. TRUST CODE (2000).

7. See generally Susan N. Gary, *UMIFA Becomes UPMIFA*, Prob. & Prop., Jan.-Feb. 2007, at 32 (Prof. Gary served as the reporter for UPMIFA).

8. UPMIFA enactment status is tracked at [www.upmifa.org/DesktopDefault.aspx?tabindex=5&tabid=68](http://www.upmifa.org/DesktopDefault.aspx?tabindex=5&tabid=68).

9. S.B. No. 411; [www.legislature.mi.gov/documents/2009-2010/billengrossed/Senate/htm/2009-SEBS-0411.htm](http://www.legislature.mi.gov/documents/2009-2010/billengrossed/Senate/htm/2009-SEBS-0411.htm). Companion bill S.B. 412 makes changes in cross references from MI-UMIFA to MI-UPMIFA in Michigan's Nonprofit Corporation Act.

10. S.B. 411 Bill Analysis, Senate Fiscal Agency (April 1, 2009); [www.legislature.mi.gov/documents/2009-2010/billanalysis/Senate/htm/2009-SFA-0411-F.htm](http://www.legislature.mi.gov/documents/2009-2010/billanalysis/Senate/htm/2009-SFA-0411-F.htm).

11. S.B. 411, § 2(d).

12. The exception for a community foundation component fund or trust is a non-UPMIFA variation in the Michigan enactment.

13. S.B. 411, § 2(e); UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 2(5) cmt. (2006).

14. S.B. 411, § 2(c).

15. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 2(3) cmt. (2006).

16. S.B. 411, § 2(b); UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 2(2) cmt. (2006).

17. S.B. 411, § 8.

18. MCL § 451.1207(1).

19. MCL § 451.1207(2).

20. MCL § 451.1205(b).

21. S.B. 411, § 3(1).

22. S.B. 411, § 3(2). The Drafting Committee's stated intent with respect to this standard is to "clarify that the same standards of prudent investing apply to all charitable institutions." UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3 cmt. (2006). The Drafting Committee sought to accomplish this by deriving the language of the prudence standard "from the RMNCA [Revised Model Nonprofit Corporation Act] and from the prudent investor rule of UPIA." *Id.*

23. S.B. 411, § 3(5)(f).

24. S.B. 411, § 3(5)(a).

25. S.B. 411, § 3(2).

26. S.B. 411, § 3(3)(a); See UNIF. PRUDENT INVESTOR ACT § 7 (1994).

27. S.B. 411, § 3(3)(b); See UNIF. PRUDENT INVESTOR ACT § 2(d) (1994).

28. S.B. 411, § 3(5)(d); See UNIF. PRUDENT INVESTOR ACT § 3 (1994)

29. S.B. 411, § 3(5)(e).

30. S.B. 411, § 3(5)(b); UNIF. PRUDENT INVESTOR ACT § 2(b) (1994).

31. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT, prefatory note (2006).

32. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3 cmt. (2006); see also Sandra L. Manzke, *Successful Investments for Foundations and Endowments – Prudent Investing for Charitable Purposes*, Tr. & Est., Dec. 1996, at 47.

33. MCL § 451.1202(d).

34. MCL § 451.1203.

35. S.B. 411, § 4(1).

36. The investment rules apply to institutional funds of all kinds, including endowment funds, but the expenditure rules apply only to endowment funds.

37. S.B. 411, § 4(1).
38. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 3(d) cmt. (2006).
39. S.B. 411, § 4(3).
40. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT, prefatory note (2006).
41. *Id.*
42. *See* UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4 cmt. (2006)
43. FINANCIAL ACCOUNTING STANDARDS BOARD, Statement of Financial Accounting Standards No. 117, ¶ 22.
44. FINANCIAL ACCOUNTING STANDARDS BOARD, Statement of Financial Accounting Standards No. 117, Appendix B: Basis for Conclusions ¶ 122-23.
45. *Id.* at ¶ 125.
46. FINANCIAL ACCOUNTING STANDARDS BOARD, FASB Staff Position FAS 117-1, Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures for all Endowment Funds. [www.fasb.org/pdf/fsp\\_fas117-1.pdf](http://www.fasb.org/pdf/fsp_fas117-1.pdf).
47. *Id.* at ¶ 6.
48. S.B. 411, § 4(1).
49. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(a) cmt. (2006).
50. Illustrative examples of these required disclosures can be found in Appendix C of FAS 117-1 on FASB's Web site, <http://www.fasb.org/>.
51. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(d) (2006).
52. *See* Joel C. Dobris, *Why Five? The Strange, Magnetic, and Mesmerizing Affect of the Five Percent Unitrust and Spending Rate on Settlers, Their Advisers, and Retirees*, 40 Real Prop. Prob. & Tr. J. 39 (2005); James Garland, *Long Duration Trusts and Endowments*, J. Portfolio Mgmt. 1 (Spring 2005); Joel C. Dobris, *Real Return, Modern Portfolio Theory, and College, University, and Foundation Decisions on Annual Spending from Endowments: A Visit to the World of Spending Rules*, 28 Real Prop. Prob. & Tr. J. 49 (1993).
53. *See* DeMarche Associates, Inc., *Spending Policies and Investment Planning for Foundations: A Structure for Determining a Foundation's Asset Mix* (Council on Foundations: 3d ed. 1999).
54. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(d) (2006).
55. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 4(d) cmt. (2006).
56. MCL § 451.1206.
57. MCL § 451.1207(1).
58. S.B. 411, § 5(1).
59. *Id.*
60. S.B. 411, § 5(3).
61. S.B. 411, § 5(2).
62. S.B. 411, § 5(4). This is not a choice of law rule. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 5 cmt. (2006).
63. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 5 cmt. (2006).
64. *Id.*
65. MCL § 451.1208(1).
66. MCL § 451.1207(2).
67. S.B. 411, § 6(1).
68. S.B. 411, § 6(2).
69. S.B. 411, § 6(3).
70. S.B. 411, § 6(4).
71. S.B. 411, §§ 6(2)-(4).
72. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 6 cmt. (2006).
73. *Id.*
74. *Id.*
75. UNIF. PRUDENT MGMT. OF INSTITUTIONAL FUNDS ACT § 6(d) cmt. (2006).
76. S.B. 411, § 6(5). The governing body of a community foundation must have the power under the foundation's governing instruments or under the applicable gift instrument to modify any restriction or condition on the distribution of funds that becomes, in effect, unnecessary, incapable of fulfillment, or inconsistent with the charitable needs of the community or area served. Treas. Reg. § 1.170A-9(e)(11)(v)(B).
77. Sgt. Phil Esterhaus, *Hill Street Blues* (1981).



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