

Memorandum

To: UMIFA Drafting Committee

From: Susan Gary, Reporter

Re: Changes from prior draft and discussion topics for the February 20-22 meeting

Date: January 29, 2004

The draft that you will receive for this meeting is a clean version and not a strike-and-score version. This memo explains the changes made to the prior draft and also raises some questions we should address at the February meeting. Unless otherwise indicated the changes made were those agreed upon at our November meeting.

This draft has been restructured. A separate section entitled Donor Intent (Section 3 in the prior draft) was deleted and the concept included where it applies.

I have substantially revised the Comments for this draft. If you have any suggestions, questions or concerns regarding the Comments, please let me know so that I can either amend the Comments or bring the questions to the Drafting Committee.

Section 2. Definitions.

(1) Charitable purpose. The term “charitable purposes” was changed from plural to singular by the Style Committee. In their view, making the term singular works better throughout the document. The Trust Code does not create a definition for charitable purpose[s] but rather says in Section 405 (titled Charitable Purposes; Enforcement) that a charitable trust may be created for one or more of the listed purposes. Our language otherwise comes from the Trust Code. The Restatement uses the plural.

(2) Endowment fund. The last sentence was added to clarify that the term does not include a board-created endowment fund established with the institution’s own assets. The Comments provide further explanation.

(3) Gift instrument. The Style Committee discussed changing the term to “donative instrument” but did not reach a recommendation as between the two terms. In November we discussed whether using the word “gift” was confusing because the term includes records that are not donative. We agreed to leave the term as it was (and as it appeared in UMIFA (1972) and include an explanation in the Comments. A choice between “gift” and “donative” does not affect our concern about whether the term is confusing.

(4) Institution. Style recommends deleting the last sentence and inserting a new second sentence so that the definition would read as follows:

“Institution” means any nonprofit corporation, trust, unincorporated association, or entity organized and operated exclusively for charitable purposes. The term includes a trust that had both charitable and noncharitable interests after the noncharitable interest ends. The term also includes a government, governmental subdivision or agency, or a governmental organization to the extent that it holds funds exclusively for a charitable purpose.

This wording is awkward because Style drafted the sentence to avoid passive voice. An alternative is the following:

A trust that has both charitable and noncharitable interests will be included in the term after the noncharitable interest ends.

I do not like any of the three options (including the version in the current draft as one of the three), so I’m looking for guidance.

(5) Institutional fund. Should this definition include a fund managed by a bank trustee?

We deleted the exclusion for programmatic investments, and we deleted the definition of programmatic investments. We decided to include all assets held by the institution within the term institutional fund but use the programmatic nature of some assets as a factor to consider in making investments or decisions to retain property. We also added a new paragraph (b) to Section 3 to make clear that an asset held for programmatic purposes may not meet the risk and return objectives otherwise applicable to the institution.

Section 3. Prudent Investing and Managing of Institutional Funds.

We streamlined subsection (a), deleting duplicative language.

A new subsection (b) addresses our concerns about programmatic investments.

We combined the section entitled “Investment Authority” (Section 5 in the prior draft) with this Section and added a number of new subsections to Section (3) from UPIA. Section 3 now more closely tracks UPIA. We agreed not to include Section 2(f) from UPIA which imposes a duty to use special skills or expertise on a trustee who has, or represents that he or she has, special skills or expertise.

Section 4. Expenditure of Endowment Funds; Rule of Construction.

Section title. The rule of construction was moved and has become subsection (a). I am uncertain about the best order for the title of this section. Rule of Construction

should probably come first because it appears first in the section, but Expenditure of Endowment Funds is the core concept of this section, so perhaps it should come first.

Should subsection (a) be applied retroactively? The Style Committee thinks that the last sentence of subsection (a), applying the rule of construction retroactively, raises “significant impairment issues.” Although a rule of construction should not be affected by impairment-of-contract concerns, interpretation of a pre-existing document under this subsection could change a donor’s understanding of the contract given that revised UMIFA no longer uses historic dollar value. That is, if a donor created an endowment under old UMIFA, language directing the charity to “pay all the income” would have been interpreted to mean that the charity could spend appreciation but could not spend below historic dollar value.

Note that the rule of construction in UMIFA (1972) applies retroactively as does the comparable provision in the newly adopted Florida statute which does not use the concept of historic dollar value.

Language in earlier drafts used the word “interpreted” which may help in making the point that this is a construction provision. The October 10, 2003 draft read:

(c) In determining the intent of a donor, a designation of a gift as an endowment, or a direction or authorization in the instrument to use only “income”, “interest”, “dividends”, or “rents, issues, or profits”, or “to preserve the principal intact”, or words of similar import, does not limit the authority to expend funds under subsection (a). Unless a gift instrument specifically limits the authority of the institution under subsection (a), the use of one of these terms shall be interpreted as the expression of the intent of the donor to create a fund that will exist in perpetuity or for a period specified by the donor. These rules of construction apply to instruments executed or in effect before or after the effective date of this [act].

The changes reflected in the current draft follow specific decisions by the drafting committee. I do not want us to rehash old issues, but I thought it might be useful to see the prior version.

Subsection (b). The lists of factors was modified to be consistent, where appropriate, with the factors in Section 3.

Subsection (d). The language for this new subsection comes from the Massachusetts statute, except that the last sentence in the Massachusetts version includes an exception for spending authorized by “the charter of the institution.” I deleted that exception. Under our draft, if a governing instrument authorizes endowment spending, the governing instrument will be part of the “gift instrument” with respect to an endowment, so the additional exclusion seemed unnecessary.

The Comment to this section explains the purpose and limited application of this subsection.

Section 5. Delegation of Investment Management.

(c) We spent a lot of time discussing appropriate wording for this subsection. The Comments explain our intentions. The Style Committee changed “an agent to whom” to “an agent to which”. UPIA uses whom, but I suppose an agent could be an investment company.

(d) In discussing subsection (d), concern was expressed that investment providers may not want to be subject to suit in some jurisdictions and may not be willing to negotiate on jurisdiction. We decided to leave the provision in because it tracks UPIA, but Carol Kroch and Sandra Champion agreed to check with people who do this to see whether the provision could create problems.

Section 6. Release or Modification or Restrictions on Use or Investment.

(a) The Style Committee wonders whether the last sentence is necessary. The sentence says, “A release is effective only upon acceptance by the institution.” Style points out that if the institution does not want to change its approach, the institution can simply continue to comply with the restriction. The release by itself does not require action by the institution. We added the sentence for this draft to bring the institution back into this provision. UMIFA (1972) provided that the institution could release a restriction, with the consent of the donor, and we changed the subsection to provide that the donor released the restriction. If the donor is the one releasing the restriction, does the institution have a role in the release? Should we delete the sentence?

The rest of this section reflects the changes agreed upon after discussion at the November meeting.

Section 7. Reviewing Compliance.

This provision comes from UPIA and was placed in a new section because it applies to sections 3 and 4. (A separate section seemed preferable to including the language in both sections 3 and 4.)

The Style Committee deleted the words “and not by hindsight” that come at the end of the provision in the UPIA version.