

Hello Susan,

I know my response is too late for your meeting, but I thought I would share my comments on the recent draft of revised UMIFA (rUMIFA). I've organized my comments on the draft into three categories: important issues, other issues, and editorial comments.

IMPORTANT ISSUES:

Section 4 permits an institution to expend so much of an endowment fund as the institution determines to be prudent, subject to the rebuttable presumption of imprudence in subsection (d) of imprudence if the institution spends more than 7% of the fair market value of the endowment fund as calculated. Do you need to make clear whether traditional income (dividends, interest, rents, royalties) becomes part of the fund or remains separate? For example, let's say a fund earns 2% of its fair market value this year as dividends and interest. Can the institution then spend 9% (2% + 7% of the fund) before triggering the imprudence test? I don't think that is your intent since that is not how most spending rate policies are implemented, but because there still are institutions that use the traditional income/principal split and spend only income, I think it would help to make that clear by stating that the total return of the fund (dividends, interest, rents, royalties, and net realized and unrealized gains and losses) is added to the fund.

I continue to worry whether the responsibility to preserve purchasing power will be observed, because a description of that responsibility does not appear in the suggested words of the act, only in the comments. States only adopt the actual words of the act; so how is that responsibility communicated to the institutions that will be applying rUMIFA?

The comments on Subsection (5) talk about program-related investments. I know this isn't the right place to discuss it, but should rUMIFA discuss whether an institution can "invest" in its own operating assets? For example, some institutions buy capital equipment or real property with interest-bearing "loans" from their endowment funds.

OTHER ISSUES:

Page 3: the definition of a gift instrument says that a solicitation can be a gift instrument "if the solicitation indicates the intent of the institution that the solicitation constitutes a gift instrument." I don't see that phraseology on solicitations I receive. (Of course, I haven't ever given big bucks. I have given to plenty of capital campaigns, however.) Would you expect that rUMIFA would change the wording on solicitations as a result of its enactment—or were you trying to describe current practice?

Page 5: I think it would be helpful to discuss the circumstances in which bylaws and minutes could be part of a gift instrument. Perhaps I am too concerned about the donor, but because a donor typically does not see these two types of documents, it seems improper that his or her gift would be subject to language in them. For example, what if the bylaws or minutes of the governing board said that for all gifts received the institution had the unilateral power to change the donor's purpose (referred to as variance power by

community foundations and accounting literature). If the donor gives without knowledge of that power and without the incorporation by reference of those minutes or bylaws should the gift be subject to them? And what about minutes of meetings or changes to the bylaws that occur after the donor's gift is given? Perhaps you could state that specific bylaw sections or minutes of a particular meeting can be one of several records constituting a gift instrument if they are incorporated by reference in one of the other records for that gift.

Page 6: I know very little about the UPIA. You say that the UPIA trustees can allocate between principal and income. Could that be a way around the problem of keeping/discarding hdv and determining how much can be spent? Could rUMIFA require that each year the governing board make a binding determination of how much of the return is added to hdv; how much is appropriated, and how much is saved for future years? I guess that wouldn't solve the underwater endowment problem, however.

Page 23, paragraph beginning on line 19: You mention that some institutions charge the cost of fundraising against an endowment fund. I've always thought that was inappropriate unless the donor was notified in advance as part of the gift instrument. Should that be explicitly stated?

Page 28, line 5-6: Sis you also consider whether this should be based on a percentage of the total assets of the institution? For some institutions, \$25,000 is a significant amount; for others \$25,000 (or even \$250,000) might be clearly insignificant.

EDITORIAL COMMENTS:

Page 3: The definition of an endowment fund contains the phrase "or any part thereof." Is that phrase still necessary now that you have removed from the definition of the fund "The term includes two or more funds collectively managed" and you have eliminated historic dollar value (hdv)? Can a single fund be part endowment and part non-endowment? If you make a change, there is a similar phrase on the page 5 comments on subsection (2).

Page 10: Should the word "contributed" or "gifted" appear before the word "property?"

Pages 13, 14, 15: References to subsection (d) should be changed to (e) because you added the ability to pool investments as (d).

Page 18, line 33 includes the words "reasonably anticipated." The words of section 4(a) do not. Is that an oversight?

You use several phrases to indicate the permanent nature of an endowment fund. In section 4(c)(1) you say "permanent." In the comments I have seen the words "maintained indefinitely," "continued indefinitely," "value of the fund endures" and "maintain its value for a long time." Do you want to standardize those phrases?

Page 23, lines 5-6 state that “endowment spending will rarely exceed seven percent,” and the following page provides several common examples of cases in which it will exceed seven percent. Perhaps you should delete or tone down that phrase.

Page 26, line 1: I don’t understand the sentence, “For many investment forms, prudence dictates diversification and diversification may best be accomplished through pooling investment vehicles which require delegation.”

Page 27: Section 6(a) states that the section applies to each fund. Is that still necessary after you removed “two or more collectively managed” from the definition of endowment fund and institutional fund? Also last sentence in the comments about subsection (a) on page 28.

Page 27: I think the first sentence would be clearer if it read, “If, because of circumstances not anticipated by the donor, a modification of a restriction contained in the gift instrument will further the purposes of the institutional fund, or a restriction contained in the gift instrument impairs the management or investment of the fund, the court, upon application of an institution, may modify that restriction. (Note that I also deleted the phrase “becomes impracticable or wasteful” since for me that made it hard to determine how subsections (c) and (d) were different.)

I also have a few questions about the cover letter that accompanied the draft.

You said that some lawyers at the ACTEC’s Charitable Planning Committee vehemently opposed a retroactive application of the rule. Can you explain what their objections were? If rUMIFA is truly more restrictive than its predecessor, their objection must not be based on a concern that the endowment will be wasted away without the hdv limitation. Is their concern based on what they believe to be an override of the donor’s intent?

You mention that some institutions began investing for ordinary income rather than long-term gain as a result of the recent market downturn. Although a change in investment philosophy might have happened if the downturn had been longer, I don’t think that was the case (although my experience is only anecdotal). Some did spend ordinary income of the funds that were underwater, but because the underwater funds generally were only a small percent of the entire investment pool, most did not change their investment philosophy, as that would have put their older appreciated funds in jeopardy in order to generate ordinary income on the fewer newer funds.

You mention that you want to ensure better reporting with respect to endowed funds. Do you believe there is a consensus on what better reporting is? If so, I would be happy to help you determine if that is possible within the current FASB guidelines. There is a lot of flexibility in the ways organizations can report, and perhaps together we can find a way to improvement.

You ask whether rUMIFA should provide for donor standing. I think that might be a good idea. During their lifetimes, donors are relatively close to the institution and to the funds that they created. Should they be unhappy with the way “their” fund is managed, the only recourse they have is to get the attention of the AG’s office. The AG may have a totally different agenda during his/her term of office (and perhaps a very limited staff and resources as well). It seems to me that giving a donor standing provides a way of resolving the issue. To prevent spurious or harassing lawsuits, could the standing be written such that the AG’s office must grant the donor the right to pursue the suit?

Thanks for allowing me to share my opinions,

Sue