

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/CS/HB 599 Uniform Prudent Management of Institutional Funds

SPONSOR(S): Civil Justice Subcommittee; Insurance & Banking Subcommittee; Passidomo

TIED BILLS: None **IDEN./SIM. BILLS:** CS/SB 952

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	14 Y, 0 N, As CS	Barnum	Cooper
2) Civil Justice Subcommittee	13 Y, 0 N, As CS	Billmeier	Bond
3) Appropriations Committee			
4) Economic Affairs Committee			

SUMMARY ANALYSIS

The Florida Uniform Management of Institutional Funds Act became law in 1990 and was updated in 2003. It is based upon the Uniform Management of Institutional Funds Act promulgated by the National Conference of Commissioners on Uniform State Laws. The Florida Uniform Management of Institutional Funds Act:

- Only applies to an institution organized and operated exclusively for educational purposes, or a governmental entity holding funds exclusively for educational purposes.
- Provides standards of conduct for a governing board.
- Delineates factors a governing board shall consider when expending endowment funds.

This bill creates the Uniform Prudent Management of Institutional Funds Act to replace the Florida Uniform Management of Institutional Funds Act. Among its key provisions, this bill:

- Makes significant enhancements to provisions currently contained in the Florida Uniform Management of Institutional Funds Act.
- Applies to all charitable institutions, not just those associated exclusively with educational purposes.
- Expands the types of assets which can be in a charitable organization's portfolio.
- Allows pooling of institutional funds for purposes of managing and investing.
- Delineates factors to be considered prior to expenditure of funds.
- Provides new procedures for releasing restrictions on small institutional funds.
- Provides for modification of restrictions on the use of endowment funds.

The provisions contained in this bill would apply to a non-educational direct-support organization only if it held a fund exclusively for charitable purposes.

This bill makes Florida's not-for-profit law consistent with national standards for the management of endowment funds which have already been adopted by 47 other states.

The fiscal impact is indeterminate.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Background

Prior to 1972, charities generally made investment and spending decisions based upon trust law guidance, which allowed for expenditure of income such as interest and dividends. Most charitable institutions invested endowment funds primarily for current income. They limited spending to a portion of dividends, interest, rents, and royalties earned. Thus, investments were predominantly made in bonds and high-yield stocks, while growth investments were avoided. The focus was on income and not capital gains. Investments were evaluated individually, rather than considering the total performance of the portfolio. At that time, trust law did not allow for delegation of investment authority.

Recognizing that charitable institutions needed guidelines separate from trust law, in 1972, the Uniform Management of Institutional Funds Act (UMIFA) was promulgated by the National Conference of Commissioners on Uniform State Laws (Uniform Law Commission).¹ The UMIFA allowed for investing in any kind of asset, pooling endowment funds for investment purposes, and delegating investment management to professional advisors. It specified that, when delegating investment management to others, a charity's governing board was required to exercise ordinary business care and prudence. UMIFA codified the first prudent investing rules. The two guiding principles were: (1) assets should be invested prudently in diversified investments that sought growth as well as income; and, (2) appreciation of assets could prudently be spent for the purposes of any endowment fund held by a charitable institution. Use of these guiding principles allowed charitable institutions to focus on the best investment strategy and distribution policy for the overall long and short-term health of the institution.

The Florida Uniform Management of Institutional Funds Act (Act) became law as a result of 1990 legislative action.² It was based upon the UMIFA. However, the State's version of UMIFA was only applicable to an institution organized and operated exclusively for educational purposes, or a governmental entity holding funds exclusively for educational purposes. The Act provided definitions and allowed for the expenditure of endowment funds by a governing board. It codified investment authority and the delegation of investment management. Consistent with UMIFA, the Act allowed for expenditure of net appreciation over the "historic dollar value"³ of the fund.

During the 2002 re-writing of the K-20 Education Code, the Act was omitted in error.⁴ When it was restored in law,⁵ the Act was updated based upon a revised draft of UMIFA issued by the Uniform Law Commission. This version provided new guidelines in response to the market situation at that time when many gifts designated for endowment had fallen below their historical market value. In that case, once an endowment had dropped below its historic gift value, all spending from the fund was stopped.

The new 2003 language in the Florida Uniform Management of Institutional Funds Act allows public and private institutions to continue to conserve the long term value of endowments while also continuing distributions consistent with the donor's wishes. The law provides guidelines for educational institutions in executing their fiduciary responsibilities by expanding and delineating factors which the governing board should consider when expending endowment funds.⁶ These include:

¹ The organization comprises more than 300 lawyers, judges and law professors, appointed by the states as well as the District of Columbia, Puerto Rico and the U.S. Virgin Islands, to draft proposals for uniform and model laws on subjects where uniformity is desirable and practicable.

² Section 1, ch. 90-297, L.O.F.

³ Per statutory definition at that time, "Historic dollar value" means the aggregate fair value in dollars of an endowment fund at the time it became an endowment fund, each subsequent donation to the fund at the time it is made, and each accumulation made pursuant to a direction in the applicable gift instrument at the time the accumulation is added to the fund.

⁴ Education K-20 Committee HB 319 w/CS Bill Analysis, page 3, dated April 8, 2003.

⁵ Section 13, ch. 2003-399, L.O.F.

⁶ Section 1010.10(3), F.S.

- The purpose of the institution.
- The intent of the donors.
- The long and short term needs of the institution.
- The general economic conditions.
- The possible effect of inflation or deflation.

Conserving the purchasing power of the endowment fund continues to be a primary goal.

The law also provides specific standards of conduct for a governing board. In addition, it identifies activities where reasonable care, skill and caution are required when delegating investment management.

The law provides additional details regarding release of restrictions placed on the use of the gift instrument or investment by the donor in the absence of the donor's written consent. The governing board is permitted to release a restriction if consent can not be obtained because of the donor's death, disability, unavailability, or impossibility of identification, if the total value was less than \$100,000 and the value was insufficient to justify separate administration. In similar circumstances, but with a value greater than \$100,000, the governing board can apply to the circuit court of the county in which the institution was located for release. In doing so, the Attorney General is required to be notified of the application and given an opportunity to be heard. The Act addresses release of restrictions, but makes no provisions for modifying a restriction.

Currently, university direct-support organizations⁷ operate in accordance with the Florida Uniform Management of Institutional Funds Act.⁸ Community college direct-support organizations are incorporated, organized and operated in a similar manner.⁹

Direct-support organizations are incorporated under the provisions of Chapter 617, F.S., and approved by the Department of State.¹⁰ In addition to university and community college direct-support organizations, the law provides that other entities, including the following, may or shall establish, create, or contract with a direct-support organization:

- Department of Elder Affairs¹¹
- Department of Juvenile Justice¹²
- Department of Legal Affairs¹³
- Department of Military Affairs¹⁴
- Department of Veterans' Affairs¹⁵
- Division of Blind Services¹⁶
- Statewide Guardian Ad Litem Office¹⁷
- Statewide Public Guardianship Office¹⁸

⁷ A university direct-support organization is a not-for-profit corporation organized and operated exclusively to receive, hold, invest, and administer property and to make expenditures to or for the benefit of a state university in Florida.

⁸ State University System of Florida Board of Governors Legislative Bill Analysis dated February 24, 2011, on file with the Insurance & Banking Subcommittee.

⁹ Section 1004.70, F.S.

¹⁰ Section 1004.28, F.S.

¹¹ Section 430.82, F.S.

¹² Section 985.672, F.S.

¹³ Section 16.616, F.S.

¹⁴ Section 250.115, F.S.

¹⁵ Section 292.055, F.S.

¹⁶ Section 413.0111, F.S.

¹⁷ Section 39.8298, F.S.

¹⁸ Section 744.7082, F.S.

The Florida Uniform Management of Institutional Funds Act is not applicable to any existing direct-support organizations associated with these entities. The Act is only applicable to an institution organized and operated exclusively for educational purposes, or a governmental entity holding funds exclusively for educational purposes.

In July 2006, the Uniform Law Commission adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA), which replaced the Uniform Management of Institutional Funds Act. UPMIFA emphasizes the portfolio approach to investing trust assets, taking into account the tradeoff between risk and return. It provides guidance and authority to charitable organizations concerning the management and investment of funds held by those organizations. UPMIFA expands the governing board's authority to delegate investment and management decisions, while clearly identifying safeguards to be observed. It applies rules on investment decision making and duties to charities organized as charitable trusts, as nonprofit corporations, or in some other manner. However, it does not apply to trusts managed by fiduciaries who are not themselves charities.

UPMIFA modernizes the rules governing expenditures from endowment funds, both to provide stricter guidelines on spending from endowment funds, and to give institutions the ability to cope more easily with fluctuations in the value of the endowment. The historic-dollar value limitation on spending from an endowment fund is replaced with rules allowing for expenditure of the principal, while requiring the board to be prudent when considering the facts and circumstances surrounding such a decision. It spells out more of the factors a charity should consider in making investment decisions,

UPMIFA updates the provisions governing the release and modification of restrictions on charitable funds to permit more efficient management of these funds. It authorizes a modification that a court determines to be in accordance with the donor's probable intention. If the charity asks for court approval of a modification, the charity must notify the state's chief charitable regulator and the regulator may participate in the proceeding.

Florida is one of only three states which have not enacted UPMIFA in some form.^{19, 20}

Effect of this Bill

This bill repeals the Florida Uniform Management of Institutional Funds Act from the Educational Codes and creates the Uniform Prudent Management of Institutional Funds Act in Chapter 617, Florida Statutes - Corporations Not for Profit. In so doing, it expands the earlier application to include charitable institutions other than those associated exclusively with educational purposes.²¹ This bill applies to any Florida not-for-profit entity meeting the definition of an "institution", which holds "institutional funds", as defined. "Institution" is defined as:

- A person, other than an individual, organized and operated exclusively for charitable purposes.
- A government or governmental subdivision, agency, or instrumentality to the extent that it holds funds exclusively for a charitable purpose.
- A trust that had both charitable and noncharitable interests after all noncharitable interests have terminated.

This bill defines "charitable purpose", which is not defined in the context of Chapter 617, as "the relief of poverty, the advancement of education or religion, the promotion of health, the promotion of a governmental purpose, or any other purpose, the achievement of which is beneficial to the community." This bill defines "institution" as:

¹⁹ Spending and Management of Endowments under UPMIFA, Findings of a 2010 Survey of Colleges, Universities, and Institutionally Related Foundations Conducted by AGB in partnership with Commonfund Institute, available at <http://www.agb.org/reports/2010/spending-and-management-endowments-under-upmifa>

²⁰ Lexology - <http://www.lexology.com/library/detail.aspx?g=f9da48c5-2fb4-45be-8f1c-4eba1eb08e05> (Last visited on March 7, 2011)

²¹ As of March 7, 2011, Department of Juvenile Justice and Department of Veterans' Affairs have reported that they currently have no endowment funds. Department of Elder Affairs has reported that the proposed legislation would have no effect on the agency.

- A person, other than an individual, organized and operated exclusively for charitable purposes;
- A government or governmental subdivision, agency, or instrumentality to the extent that it holds funds exclusively for a charitable purpose; or
- A trust that had both charitable and noncharitable interests after all noncharitable interests have terminated.

This bill defines "institutional fund" as a fund held by an institution exclusively for charitable purposes. The term does not include:

- Program-related assets;
- A fund held for an institution by a trustee that is not an institution;
- 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; or
- A fund managed or administered by the State Board of Administration pursuant to its constitutional or statutory authority.

This bill makes significant enhancements to provisions previously contained in the Florida Uniform Management of Institutional Funds Act. Among its key provisions, this bill:

- Expands the types of assets which can be in a charitable organizations portfolio, to include any kind of property or type of investment consistent with the new statutes.
- Specifies that management and investment of institutional funds must be accomplished with the care an ordinarily prudent person would exercise.
- Requires an institution to make a reasonable effort to verify relevant facts.
- Allows pooling of institutional funds for purposes of managing and investing.
- Makes reference to an overall investment strategy for the first time.
- Obliges a person with special relevant skills or expertise, to use those skills or that expertise in managing and investing institutional funds.
- Delineates factors to be considered prior to expenditure of funds.

While current law makes no provision for modifying a restriction, and limits a governing board's ability to release restrictions without petitioning the court, this bill provides for more flexibility, while protecting the donor's interest and intent. In addition to seeking release because a restriction is unlawful, impractical, or wasteful, the new procedures allow for modification or release of a restriction because of circumstances not anticipated by the donor. For funds with a value of \$100,000 or less, notification of the Attorney General is still required. In those situations where the institutional fund subject to the restriction has a total value of \$100,000 to \$250,000, and more than 20 years has elapsed since the fund was established, the governing board must provide written notice to the Attorney General prior to modification or release of the restriction.

The rules and guidelines contained in this bill apply to future decisions or actions taken on institutional funds already held and all new funds established after the effective date of this bill. This conforms to national standards.

This bill provides for an exception to the Electronic Signatures in Global and National Commerce Act (ESIGN), 15 U.S.C. § 7001.²² Per 15 U.S.C. § 7002, in some cases exceptions are permissible if a state has enacted the Uniform Electronic Transactions Act, which Florida did in 2000.²³ The exception does not result in any loss of the consumer protections contained in the ESIGN. This bill's provisions

²² This section provides that a signature, contract, or other record relating to such transaction may not be denied legal effect, validity, or enforceability solely because it is in electronic form; and a contract relating to such transaction may not be denied legal effect, validity, or enforceability solely because an electronic signature or electronic record was used in its formation. It also provides consumer protections.

²³ Section 1, ch. 2000-164, L.O.F.

regarding the relation to ESIGN is consistent with the UPMIFA and incorporated in similar laws of other states.

This bill makes Florida's not-for-profit law consistent with national standards for the management of endowment funds already adopted by 47 other states.

This bill provides an effective date of July 1, 2012.

B. SECTION DIRECTORY:

Section 1 creates s. 617.2104, F.S., relating to the Uniform Prudent Management of Institutional Funds Act.

Section 2 repeals s. 1010.10, F.S., relating to the Florida Uniform Management of Institutional Funds Act.

Section 3 provides an effective date of July 1, 2012.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Indeterminate.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or, reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

At the March 9, 2011, meeting of the Insurance & Banking Subcommittee, four amendments were proposed and adopted.

Amendment 1 provided that funds administered by the State Board of Administration are not subject to the provisions of this bill.

Amendment 2 clarified that the circuit court for the circuit in which an institution is located is the appropriate court to handle requests for changes to restrictions. It removed the requirement that the Attorney General be provided an opportunity to respond to requests for modifications.

Amendment 3 removed the requirement that the Attorney General approve requests to release or modify restrictions for funds with a value of \$100,000 to \$250,000.

Amendment 4 changed the effective date to July 1, 2012.

The Civil Justice Subcommittee considered the bill on March 29, 2011, and adopted an amendment to correct a statutory cross-reference. The bill, as amended, was reported favorably as a committee substitute. This analysis reflects the committee substitute as reported by the Civil Justice Subcommittee.