

BILL ANALYSIS

C.S.H.B. 860
By: Paxton
State Affairs
Committee Report (Substituted)

BACKGROUND AND PURPOSE

The Uniform Management of Institutional Funds Act (UMIFA) was adopted by the Texas Legislature in 1989. UMIFA was developed by the National Conference of Commissioners on Uniform State Laws (NCCUSL) in 1972. This law has provided guidance and authority to charitable organizations concerning the management and investment of funds held by those organizations.

This bill replaces UMIFA with the Uniform Prudent Management of Institutional Funds Act (UPMIFA) which was adopted by the NCCUSL in 2006. Because prudence norms have evolved since the 1970s, UPMIFA provides modern articulations of the prudence standards for the management and investment of charitable funds and for endowment spending.

UPMIFA reflects the fact that standards for managing and investing institutional funds are and should be the same regardless of whether a charitable organization is organized as a trust, a nonprofit corporation, or some other entity. UPMIFA provides guidance and authority to charitable organizations concerning the management and investment of funds held by those organizations, and UPMIFA imposes additional duties on those who manage and invest charitable funds. These duties provide additional protections for charities and also protect the interests of donors who want to see their contributions used wisely.

Highlights of UPMIFA include the following:

- 1.) It expressly enumerates factors a charity should consider in making investment decision, including preservation of the endowment fund.
- 2.) It improves the protection of donor intent.
- 3.) It improves the endowment spending rule by eliminating the concept of historic dollar value and providing better guidance regarding the operation of the prudence standard.
- 4.) It includes a presumption of imprudence if a charity spends more than seven percent of the endowment in any one year or more than five percent for small endowments. The presumption is meant to protect against spending an endowment too quickly.
- 5.) It clarifies that the doctrines of cy pres and deviation apply to funds held by nonprofit corporations as well as to funds held by charitable trusts but gives charities broader authority to modify restrictions on a fund that is both old and small permitting the charity to make appropriate modifications and avoid the expense of a court hearing. In all instances the attorney general continues to be the protector both of the donor's intent and of the public's interest in charitable funds.

RULEMAKING AUTHORITY

It is the committee's opinion that this bill does not expressly grant any additional rulemaking authority to a state officer, department, agency, or institution.

ANALYSIS

SECTION 1 strikes Chapter 163, Property Code, and inserts a new chapter.

Sec. 163.001 establishes the name of the chapter.

Sec. 163.002 states legislative findings and purpose.

Sec. 163.003 defines (1) “charitable purpose,” (2) “endowment fund,” (3) “gift instrument,” (4) “institution,” (5) “institutional fund,” (6) “person,” (7) “program-related asset,” and (8) “record.”

Sec. 163.004 adopts the prudence standard for investment decision making, using a portfolio approach and considering the risk and return objectives of the fund.

Sec. 163.004(a) expresses the overarching duty to comply with donor intent while requiring the consideration of the charitable purposes of the institution.

Sec. 163.004(b) reminds fund managers that the duty of loyalty will apply to their actions while requiring fund managers to manage and invest in good faith and with the care of an ordinarily prudent person.

Sec. 163.004(c) authorizes an institution to minimize costs and to investigate the accuracy of the information used in making management decisions.

Sec. 163.004(d) authorizes an institution to pool funds for management and investment purposes.

Sec. 163.004(e) provides that a set of criteria be considered if an institutional fund is to be managed and invested. Provides that the context of the institutional fund's portfolio of investments as a whole or as a part of an overall investment strategy be considered if a decision about an individual asset is to be made. Authorizes an institution to invest in any kind of property or investment in accordance with the law. Requires an institution to diversify the investment fund unless the purposes of the fund are better served without diversification. Requires an institution to make a decision on whether to retain or rebalance the institutional fund portfolio within a reasonable time when receiving property. States that a managing and investing person has a duty to use their skills and expertise.

Sec. 163.005 replaces the existing prudence standard which relied on the historic dollar value of the fund. Instead, this section applies a prudence standard which would generate sufficient gains in the fund to be able to make ongoing distributions from the fund while at the same time preserving the purchasing power of the fund. Determining spending would be based on the total assets of the endowment fund.

Sec. 163.005(a), subject to the intent of a donor and the established rebuttable presumption of imprudence depending on the funds value, authorizes an institution to appropriate or accumulate funds and requires the consideration of certain prudence factors while acting in good faith and with care. Assumes that all endowment funds are donor-restricted unless a gift states otherwise.

Sec. 163.005(b) provides that fund managers are authorized to determine expenditure and accumulation levels as they determine are prudent if the gift instrument has not specifically stated a limitation.

Sec. 163.005(c) provides rules of construction to assist institutions in interpreting donor's intent.

Sec. 163.005(d) establishes a rebuttable presumption of imprudence for funds over \$1 million if an institution spends more than seven percent (7%) of the fair market value of the fund as determined from the immediately preceding three years. Provides that the fair market value of the endowment fund be calculated for the period the fund has been in existence if it has been in existence for less than three years.

Sec. 163.005(e) establishes a rebuttable presumption of imprudence for funds under \$1 million if an institution spends more than five percent (5%) of the fair market value of the fund as determined from the immediately preceding three years. Provides that the fair market value of the endowment fund be calculated for the period the fund has been in existence if it has been in existence for less than three years.

Sec. 163.005(f) stipulates that Sec. 163.005 would not apply to individual funds in a pooled fund or to funds managed under a collective investment policy. Rather, the prudence standards and the presumption of imprudence would apply to the entire pool or collective investment policy.

Sec. 163.006 establishes guidelines for the delegation of management and investment functions.

Sec. 163.006(a) authorizes an institution to delegate management and investment functions to external agents. Requires an institution to exercise reasonable skill, care, and caution in selecting the agent, defining the scope of the delegation, and reviewing the performance of the agent.

Sec. 163.006(b) provides that an agent performing a delegated function exercise reasonable care to comply with the scope and terms of the delegation.

Sec. 163.006(c) provides that an institution exercising reasonable skill, care, and caution in selecting the agent, defining the scope of the delegation, and reviewing the performance of the agent, is not liable for the decisions or actions of an agent.

Sec. 163.006(d) provides that an agent accepting a delegated function submits to the jurisdiction of the courts of this state in all proceedings arising from or related to the delegated function.

Sec. 163.006(e) Authorizes an institution to delegate management and investment functions to its committees, officers, and employees.

Sec. 163.007 expresses the releasing or modifying restrictions placed on a trust.

Sec. 163.007(a) authorizes an institution to modify a restriction with donor consent. Prohibits a release or modification for non-charitable purposes of the institution.

Sec. 163.007(b) authorizes a court to modify restrictions contained in a gift instrument without donor consent through a court order when trust restrictions become impractical or wasteful. Provides that the modification be made in accordance with the donor's probable intention. Applies the attorney general's participation in proceedings involving charitable trusts.

Sec. 163.007(c) authorizes a court to modify the purpose of a gift instrument if the purpose becomes unlawful, impracticable, impossible to achieve, or wasteful. Applies the attorney general's participation in proceedings involving charitable trusts.

Sec. 163.007(d) authorizes an institution to modify a restriction contained in a gift instrument that becomes unlawful, impracticable, impossible to achieve, or wasteful, after appropriate notice has been given to the attorney general if the fund's value is less than \$25,000, is more than 20 years old, and is used in the manner expressed in the gift instrument.

Sec. 163.007(e) provides that a copy of the gift instrument and a statement of facts showing that the fund's value is less than \$25,000, is more than 20 years old, and is used in the manner expressed in the gift instrument, accompany notification of the attorney general.

Sec. 163.008 does not allow hindsight to replace facts and circumstances in determining compliance with the management, investment, and expenditure of institutional funds.

Sec. 163.009 establishes the applicability of the provisions of the Electronic Signatures in Global and National Commerce Act (15 U.S.C. Section 7001).

Sec. 163.010 provides that the promotion of uniformity of the law be considered in applying the act if other states have similar statutes.

Sec. 163.011 exempts funds subject to this chapter from the provisions of Subtitle B, Title 9 (the Texas Trust Code).

SECTION 2 amends the Education Code to make the terms conform to the language of the Chapter 163, Property Code. Authorizes the State Board of Education to delegate investment authority to the same extent as an institution.

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SECTION 4 amends the Education Code to make the terms conform to the language of the Chapter 163, Property Code. Defines "institution" and "institutional fund."

SECTION 5 applies the changes made by the Act to institutional funds existing on or established after the effective date. Applies the changes made by the Act to an action taken or decision made after August 31, 2007, for an institutional fund existing on the effective date.

SECTION 6 makes the Act effective September 01, 2007

EFFECTIVE DATE

September 1, 2007.

COMPARISON OF ORIGINAL TO SUBSTITUTE

The substitute is identical to the original bill except for the insertion of Sec. 163.005(d), (e), and (f), which establish the 'bright line standard' of the rebuttable presumption of imprudence at 7% for large funds and 5% for small funds. Additionally, this insertion of language applies Sec. 163.005 to an entire pool or collective investment policy of funds rather than to individual funds within a pool or collective investment policy.