NEW JERSEY ADOPTS THE UNIFORM PRUDENT MANAGEMENT OF INSTITUTIONAL FUNDS ACT

New Jersey recently adopted the Uniform Prudent Management of Institutional Funds Act (UPMIFA), replacing the 1975 Uniform Management of Institutional Funds Act (UMIFA). Both UPMIFA and UMIFA provide rules for how certain wholly charitable institutions, including hospitals, universities and their foundations, should make investment decisions for both their endowment and non-endowment assets. In addition, at the time it was enacted, UMIFA created new standards that increased the ability of an institution to spend from an endowment. The act, however, also placed limitations on charitable institutions that made it difficult to make distributions from endowment assets during a period that an endowment is worth less than the value of the assets that have been contributed to it. UPMIFA adopts an approach that allows a charitable institution's board to spend money from an endowment fund as long as the decision to spend is financially prudent and consistent with donor intent.

While UMIFA contained a general obligation to invest prudently using ordinary business care, UPMIFA updates the prudence standard to adopt more modern practices and provide greater guidance to boards by imposing the following duties:

1. Give primary consideration to donor intent as expressed in a gift instrument;
2. Act in good faith, with the care an ordinarily prudent person would exercise;
3. Incur only reasonable costs in investing and managing institutional funds;
4. Make a reasonable effort to verify relevant facts;
5. Make decisions about each asset in the context of the portfolio of investments as part of an overall investment strategy;
6. Diversify investments, unless due to special circumstances, the purposes of the fund are better served without diversification;
7. Dispose of unsuitable assets; and
8. In general, develop an investment strategy appropriate for the fund and the institution.

Thus, it is of central importance that the boards of charitable institutions managing funds for charitable purposes adopt an appropriate investment strategy in light of the new law.

In today's economic climate, perhaps the most important change made by UPMIFA is the adoption of a flexible approach to spending that allows institutions to deal with fluctuations in the value of an endowment. Under UMIFA, an institution was limited to spending the appreciation in an endowment fund above the "historic dollar value" of the fund – the total worth of the gift at creation plus any subsequent additions of the fund. There was no clear guidance as to what the board could do if the fund dropped below the historic dollar value, something that has happened to a number of charitable funds during the recent market declines in 2000 to 2001, and in 2008. UPMIFA eliminates references to the historic dollar value. Instead, UPMIFA allows fund managers to spend from a fund, as long as such spending is in accordance with the new prudent spending requirements, including the requirement that it be consistent with donor intent.

UPMIFA also contains provisions permitting the release and modification of donor restrictions on funds held by charitable institutions in certain circumstances. Under both UMIFA and UPMIFA, a donor can release a restriction the donor imposed on a charitable gift. Under UMIFA, if the board cannot obtain the donor's consent, perhaps because the donor is dead, the institution can go to court to release or modify restrictions that are obsolete, inappropriate, or impracticable. Institutions either had to spend a great deal of money to obtain court approval to release or modify such restriction or allow the fund to languish. Rather than permit the release of a restriction with no limitations on future use, UPMIFA adopts the doctrines of cy pres and deviation. Applying deviation, UPMIFA allows an institution to petition a court to modify or release a restriction that has become impracticable, wasteful, impairs the management or investment of the fund or, if because of circumstances unanticipated by the donor, the modification will further the purposes of the fund. Any change must be consistent with the donor's probable intention. UPMIFA also applies cy pres and allows a change if consistent with the charitable purpose of the institution or charitable intent of the donor. In addition, UPMIFA adds a new provision that should be helpful to institutions that have restrictions on old and relatively small funds. Under UPMIFA, institutions can now make modifications to restrictions on funds that are both under $250,000 and have been established for at least 20 years without going to court, provided that the institution must continue to use the property in a manner consistent with the donor's charitable purpose expressed in the gift instrument. In order to modify a restriction without going to court, the institution must give 60 days notice of the proposed modification to the State Attorney General. This provision helps resolve the problem that occurs with restrictions that have outlived their purpose, but are too small to justify the costs of going to court.

For more information on UPMIFA, please contact any of our Wealth Advisors or your regular Artisan Wealth Management, LLC contact.

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Telephone - (908) 366-7630 | Fax - (908) 366-7639 | Toll Free - (800) 769-6590
www.artisanwealthmanagement.com