

1975 Senate Bill 238

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CHAPTER 247, Laws of 1975

AN ACT to create 112.07 of the statutes, relating to establishment of guidelines for the management and use of investments held by eleemosynary institutions and funds.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

112.07 of the statutes is created to read:

112.07 Uniform management of institutional funds act. (1) DEFINITIONS. In this section:

(a) "Institution" means an incorporated or unincorporated organization organized and operated exclusively for educational, religious, charitable, or other eleemosynary purposes, or a governmental organization to the extent that it holds funds exclusively for any of these purposes.

COMMISSIONERS' NOTE: The Uniform Act applies generally to colleges, universities, hospitals, religious organizations and other institutions of an eleemosynary nature. It applies to a governmental organization to the extent that the organization holds funds for the listed purposes, e.g., a public school which has an endowment fund.

A nongovernmental institution which is not "charitable" in the classic sense is not within the Act, even though it may hold funds for such purpose. If the fund is separate and distinct from the noncharitable organization, the fund itself may be an institution to which the Act applies.

(b) "Institutional fund" means a fund held by an institution for its exclusive use, benefit, or purposes, but does not include 1) a fund held for an institution by a trustee that is not an institution or 2) a fund in which a beneficiary that is not an institution has an interest, other than possible rights that could arise upon violation or failure of the purposes of the fund.

COMMISSIONERS' NOTE: An institutional fund is any fund held by an institution which it may invest for a long or short term. Excluded from the Act is any fund held by a trustee which is not an institution as defined in this Act, e.g., a bank or trust company, for the benefit of an institution even though the institution is the sole beneficiary.

A fund held by an institution for the benefit of any noninstitutional beneficiary is also excluded. The exclusion would apply to any fund with an individual beneficiary such as an annuity trust or a unitrust. When the interest of a noninstitutional beneficiary is terminated, the fund may then become an institutional fund.

The “use, benefit, or purposes” of an institution broadly encompasses all of the activities permitted by its charter or other source of authority. A fund to provide scholarships for students or medical care for indigent patients is held by the school or hospital for the institution’s purposes. Such a fund is not deemed to be held for the benefit of a particular student or patient as distinct from the use, benefit, or purposes of the institution, nor does the student or patient have an interest in the fund as a “beneficiary which is not an institution”.

The particular recipient of the aid of a charitable organization is not a “beneficiary” in the sense of a beneficiary of a private trust; only the Attorney General or similar public authority may enforce a charitable trust. 4 Scott, Law of Trusts s. 348 pp. 2768-9 (3d ed. 1967); Bogert, The Law of Trusts and Trustees s. 411-15 pp. 317-348 (2d ed. 1962).

(c) “Endowment fund” means an institutional fund, or any part thereof, not wholly expendable by the institution on a current basis under the terms of the applicable gift instrument.

COMMISSIONERS’ NOTE: An endowment fund is an institutional fund, or any part thereof, which is held in perpetuity or for a term and which is not wholly expendable by the institution. Implicit in the definition is the continued maintenance of all or a specified portion of the original gift. “Endowment fund” is specially defined because it is subject to the appropriation rules of sub. (2).

A restriction on use that makes a fund an endowment fund arises only from the applicable gift instrument. If a governing board has the power to spend all of a fund but, in its discretion, decides to invest the fund and spend only the yield or appreciation therefrom, the fund does not become an endowment fund under this definition, but it may be described as a “quasi-endowment fund” or a “fund functioning as endowment”.

A fund which is not an institutional fund originally and therefore not an endowment fund may become an endowment fund at a later time. For example, a fund given to an institution to pay the grantor’s widow a life income, with the remainder to the institution, would become an institutional fund on the widow’s death, and, if the fund were not then wholly expendable, it would become an endowment fund at that time.

If a gift instrument provided that the institution could use the income from the fund for ten years and thereafter spend the entire principal, the fund would be an endowment fund for the ten-year period and would cease to be an endowment fund at the time it became wholly expendable.

(d) “Governing board” means the body responsible for the management of an institution or of an institutional fund.

COMMISSIONERS’ NOTE: The definition is meant to designate the policy making or management group which has the responsibility for the affairs of the institution or the fund.

(e) “Historic dollar value” means the aggregate fair value in dollars of 1) an endowment fund at the time it became an endowment fund, 2) each subsequent donation to the fund at the time it is made, and 3) each accumulation made pursuant

to a direction in the applicable gift instrument at the time the accumulation is added to the fund. The determination of historic dollar value made in good faith by the institution is conclusive.

COMMISSIONERS' NOTE: "Historic dollar value" is simply the value of the fund expressed in dollars at the time of the original contribution to the fund plus the dollar value of any subsequent gifts to the fund. Accounting entries recording realization of gains or losses to the fund have no effect upon historic dollar value. No increase or decrease in historic dollar value of the fund results from the sale of an asset held by the fund and the reinvestment of the proceeds in another asset.

If the gift instrument directs accumulation, the historic dollar value will increase with each accumulation. For example, if a donor gives an institution \$300,000 and directs that the fund is to be accumulated until its value reaches \$500,000, the historic dollar value will be the aggregate value of \$500,000 at the time the fund becomes available for use by the institution.

If under the terms of the gift instrument a portion of an endowment fund, after passage of time or upon the happening of some event, becomes currently wholly expendable, such portion should be treated as a separate fund and the historic dollar value of the remaining endowment fund should be reduced proportionately.

(f) "Gift instrument" means a will, deed, grant, conveyance, agreement, memorandum, writing, or other governing document (including the terms of any institutional solicitations from which an institutional fund resulted) under which property is transferred to or held by an institution as an institutional fund.

COMMISSIONERS' NOTE: A gift instrument establishes the terms of the gift. It may be a writing of any form, or it may result from the institution's solicitation activities, or the bylaws, or other rules of an existing fund.

(2) **APPROPRIATION OF APPRECIATION.** The governing board may appropriate for expenditure for the uses and purposes for which an endowment fund is established so much of the net appreciation, realized and unrealized, in the fair value of the assets of an endowment fund over the historic dollar value of the fund as is prudent under the standard established by sub. (6). This subsection does not limit the authority of the governing board to expend funds as permitted under other law, the terms of the applicable gift instrument, or the charter of the institution.

COMMISSIONERS' NOTE: This subsection authorizes a governing board to expend for the purposes of the fund the increase in value of an endowment fund over the fund's historic dollar value, within the limitations of sub. (6) which establishes a standard of business care and prudence.

The subsection does not apply to funds which are wholly expendable by the institution such as so-called "quasi-endowment funds" or "funds functioning as endowment," nor does the section limit or reduce any spending power granted by a gift instrument or otherwise held by the institution.

Unrealized gains and losses must be combined with realized gains and losses to insure that the historic dollar value is not impaired.

(3) **RULE OF CONSTRUCTION.** Subsection (2) does not apply if the applicable gift instrument indicates the donor's intention that net appreciation shall not be expended. A restriction upon the expenditure of net appreciation may not be implied from a designation of a gift as an endowment, or from a direction or authorization in the applicable gift instrument to use only "income", "interest", "dividends", or "rents, issues or profits", or "to preserve the principal intact", or a direction which contains

other words of similar import. This rule of construction applies to gift instruments executed or in effect before or after the effective date of this act (1975).

COMMISSIONERS' NOTE: If a gift instrument expresses or otherwise indicates the donor's intention that the governing board may not appropriate the appreciation in the value of the fund, his wishes will govern.

The rule of construction of this subsection is based upon the assumption that a grantor who makes an outright gift to an educational, religious, charitable or other eleemosynary institution seldom makes a full statement of his intentions and that his unstated intention is usually quite different from the intention of a grantor who makes a gift to a trust for private beneficiaries. The assumption is that the grantor of a gift to an institution: (1) means to devote to the institution any return or benefit that the institution can obtain from the gift, (2) acknowledges the responsibility of the institutional management to determine the prudent use of the return or benefit over time and (3) usually regards the "amount" of the gift as the dollars given or the dollar value of the property transferred to the institution at the time of the gift. Thus, in the case of a gift instrument which states no clear intention or merely echoes the rubrics of a private trust, the statutory rule of interpretation should apply.

Some advisers to institutions, aware of the body of private trust law, have interpreted references to "income" or "principal" in a gift instrument to evidence a grantor's intent that the private trust rules developed to insure equity between an income beneficiary and a remainderman should be applied to an outright gift to an institutional donee. Neither the facts of donor's intentions nor the law of trusts support such an interpretation of the meaning of gift instruments where an institution is the sole beneficiary.

This subsection does not purport to change existing law or rights; it simply codifies a rule of construction or interpretation or administration by articulating the presumed intent of a donor in the absence of a statement of the donor's actual intent.

(4) **INVESTMENT AUTHORITY.** In addition to an investment otherwise authorized by law or by the applicable gift instrument, and without restriction to investments a fiduciary may make, the governing board, subject to any specific limitations set forth in the applicable gift instrument or in the applicable law other than law relating to investments by a fiduciary, may:

(a) Invest and reinvest an institutional fund in any real or personal property deemed advisable by the governing board, whether or not it produces a current return, including mortgages, stocks, bonds, debentures, and other securities of profit or nonprofit corporations, shares in or obligations of associations, partnerships, or individuals, and obligations of any government or subdivision or instrumentality thereof;

(b) Retain property contributed by a donor to an institutional fund for as long as the governing board deems advisable;

(c) Include all or any part of an institutional fund in any pooled or common fund maintained by the institution; and

(d) Invest all or any part of an institutional fund in any other pooled or common fund available for investment, including shares or interests in regulated investment companies, mutual funds, common trust funds, investment partnerships, real estate investment trusts, or similar organizations in which funds are commingled and investment determinations are made by persons other than the governing board.

COMMISSIONERS' NOTE: Institutional investment managers suggest that a general grant of investment powers will clarify the authority of a governing board to select investments. Paragraph (a) provides broad powers of investment and states that a governing board is not restricted to investments authorized to trustees.

Two other matters of investment policy have been troublesome to boards because of the absence of specific authority. Paragraphs (b) and (c) provide authority to hold property given by a donor even though it may not be the best investment (ordinarily in the hope of obtaining additional contributions) and to invest in common or pooled investment funds such as the Common Fund for Nonprofit Organizations. See 4 Scott, Law of Trusts s. 389 pp. 2997-3000 (3d ed. 1967).

The absence of specific reference to investment for return by an institution in its own facilities does not limit the power of a governing board to make such investments under the general clause of sub. (4) (a), or other law or the gift instrument.

Subsection (6) establishes the standard of care and prudence under which the investment authority is exercised.

(5) DELEGATION OF INVESTMENT MANAGEMENT. Except as otherwise provided by the applicable gift instrument or by applicable law relating to governmental institutions or funds, the governing board may a) delegate to its committees, officers or employees of the institution or the fund, or agents, including investment counsel, the authority to act in place of the board in investment and reinvestment of institutional funds, b) contract with independent investment advisors, investment counsel or managers, banks, or trust companies, so to act, and c) authorize the payment of compensation for investment advisory or management services.

COMMISSIONERS' NOTE: Questions have arisen about the power of a governing board to delegate investment decisions. In the absence of authority, some boards have tried to follow the nondelegation principles applicable to trustees. Governing boards do, in fact, delegate investment authority, sometimes with rather cumbersome procedures to produce a record of apparent decisions by the boards.

This subsection clarifies the authority to delegate investment management and to purchase investment advisory and management services. Responsibility for investment policy and selection of competent agents remains with the board under the sub. (6) standard of business care and prudence.

(6) STANDARD OF CONDUCT. In the administration of the powers to appropriate appreciation, to make and retain investments, and to delegate investment management of institutional funds, members of a governing board shall exercise ordinary business care and prudence under the facts and circumstances prevailing at the time of the action or decision. In so doing they shall consider long and short term needs of the institution in carrying out its educational, religious, charitable, or other eleemosynary purposes, its present and anticipated financial requirements, expected total return on its investments, price level trends, and general economic conditions.

COMMISSIONERS' NOTE: This subsection establishes a standard of care and prudence for a member of a governing board. The standard is generally comparable to that of a director of a business corporation rather than that of a private trustee, but it is cast in terms of the duties and responsibilities of a manager of a nonprofit institution.

Officers of a corporation owe a duty of care and loyalty to the corporation, and the more intimate the knowledge of the affairs of the corporation the higher the standard of care. Directors are obligated to act in the utmost good faith and to exercise ordinary business care and prudence in all matters affecting the management of the corporation. This is a proper standard for the managers of a nonprofit institution, whether or not it is incorporated.

The standard of sub. (6) was derived in part from Proposed Treasury Regulations s. 53.4944-1 (a) (2) dealing with the investment responsibility of managers of private foundations.

The standard requires a member of a governing board to weigh the needs of today against those of the future.

(7) **RELEASE OF RESTRICTIONS ON USE OR INVESTMENT.** (a) With the written consent of the donor, the governing board may release, in whole or in part, a restriction imposed by the applicable gift instrument on the use or investment of an institutional fund.

(b) If written consent of the donor cannot be obtained by reason of his death, disability, unavailability, or impossibility of identification, the governing board may apply in the name of the institution to the county or circuit court for release of a restriction imposed by the applicable gift instrument on the use or investment of an institutional fund. The attorney general shall be notified of the application and shall be given an opportunity to be heard. If the court finds that the restriction is obsolete, inappropriate, or impracticable, it may by order release the restriction in whole or in part. A release under this paragraph may not change an endowment fund to a fund that is not an endowment fund.

(c) A release under this subsection may not allow a fund to be used for purposes other than the educational, religious, charitable, or other eleemosynary purposes of the institution affected.

(d) This subsection does not limit the application of the doctrine of cy pres.

COMMISSIONERS' NOTE: One of the difficult problems of fund management involves gifts restricted to uses which cannot be feasibly administered or to investments which are no longer available or productive. There should be an expeditious way to make necessary adjustments when the restrictions no longer serve the original purpose. Cy pres has not been a satisfactory answer and is reluctantly applied in some states. See Restatement of Trusts (2d), ss. 381, 399; 4 Scott, Law of Trusts s. 399 p. 3084, s. 399.4 pp. 3119 et seq. (3d ed. 1967).

This subsection permits a release of limitations that imperil efficient administration of a fund or prevent sound investment management if the governing board can secure the approval of the donor or the appropriate court.

Although the donor has no property interest in a fund after the gift, nonetheless if it is the donor's limitation that controls the governing board and he or she agrees that the restriction need not apply, the board should be free of the burden. See Restatement of Trusts (2d) s. 367. Scott suggests that in minor matters, the consent of the settlor may be effective to remove restrictions upon the trustees in the administration of a charitable trust. 4 Scott, s. 367.3 p. 2846 (3d ed. 1967).

If the donor is unable to consent or cannot be identified, the appropriate court may upon application of a governing board release a limitation which is shown to be obsolete, inappropriate or impracticable.

This subsection authorizes only a release of a limitation. Thus, if a fund were established to provide scholarships for students named Brown from Brown County, Iowa, a donor might acquiesce in a reduction of the limitation to enable the institution to offer scholarships to students from Brown County who are not named Brown, or to students from other counties in Iowa or to students from other states, or he could acquiesce in the release of the restriction to scholarships so that the fund could be used for the general educational purposes of the school.

Paragraph (d) makes it clear that the Act does not purport to limit the established doctrine of cy pres. A liberalization of, addition to, or substitute for cy pres is not without respectable support. Professor Kenneth Karst in "The Efficiency of the Charitable Dollar: An Unfilled State Responsibility", 73 Harv. L. Rev. 433 (1960) suggested that the doctrine of cy pres be expanded to permit the courts to redirect charitable grants if the purpose had become "obsolete, or useless, or prejudicial to the public welfare, or are insignificant in comparison with the magnitude of the endowment. . ." quoting from the Nathan Report (of the British Committee on the Law and Practice Relating to Charitable Trusts, Cmd. 8710, 1952) quoting the Scotland Education Act 1946, 9-10 Geo. 6, ch. 72 s. 119 (b). The Uniform Act provision is far less broad; it applies only to the release of restrictions on the gift under limited circumstances.

New England courts apply a rather strict doctrine of separation of powers to deny legislative encroachment on judicial cy pres. The Act is compatible with the New England cases because the final decision is in the courts. See City of Hartford v. Larrabee Fund Association, 161 Conn. 312, 288 A. 2d 71 (1971); Opinion of Justices, 101 N.H. 531, 133 A. 2d 792 (1957).

No federal tax problems for the donor are anticipated by permitting release of a restriction. The donor has no right to enforce the restriction, no interest in the fund and no power to change the eleemosynary beneficiary of the fund. He may only acquiesce in a lessening of a restriction already in effect.

(8) UNIFORMITY OF APPLICATION AND CONSTRUCTION. This section shall be so applied and construed as to effectuate its general purpose to make uniform the law with respect to the subject of this section among those states which enact it.

(9) SHORT TITLE. This section may be cited as the "Uniform Management of Institutional Funds Act".
