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(FORM UPDATED: 08/11/2010)

WISCONSIN STATE LEGISLATURE ...
PUBLIC HEARING - COMMITTEE RECORDS

1995-96

(session year)

Assembly

(Assembly, Senate or Joint)

Committee on Insurance, Securities and Corporate Policy...

COMMITTEE NOTICES ...

- Committee Reports ... CR
- Executive Sessions ... ES
- Public Hearings ... PH

INFORMATION COLLECTED BY COMMITTEE FOR AND AGAINST PROPOSAL

- Appointments ... Appt (w/Record of Comm. Proceedings)
- Clearinghouse Rules ... CRule (w/Record of Comm. Proceedings)
- Hearing Records ... bills and resolutions (w/Record of Comm. Proceedings)
  (**ab** = Assembly Bill) (**ar** = Assembly Resolution) (**ajr** = Assembly Joint Resolution)
  (**sb** = Senate Bill) (**sr** = Senate Resolution) (**sjr** = Senate Joint Resolution)
- Miscellaneous ... Misc

* Contents organized for archiving by: Stefanie Rose (LRB) (October 2012)

WISCONSIN LEGISLATIVE COUNCIL STAFF MEMORANDUM

One East Main Street, Suite 401; P.O. Box 2536; Madison, WI 53701–2536
Telephone (608) 266–1304
Fax (608) 266–3830

DATE: November 8, 1995

TO: MEMBERS OF THE ASSEMBLY COMMITTEE ON INSURANCE, SECURITIES AND CORPORATE POLICY

FROM: Gordon A. Anderson, Senior Staff Attorney

SUBJECT: Materials Related to 1995 Assembly Bill 285, Relating to Regulating the Investments of Trustees

On October 19, 1995, the Assembly Committee on Insurance, Securities and Corporate Policy held a public hearing on Assembly Bill 285, relating to regulating the investments of trustees.

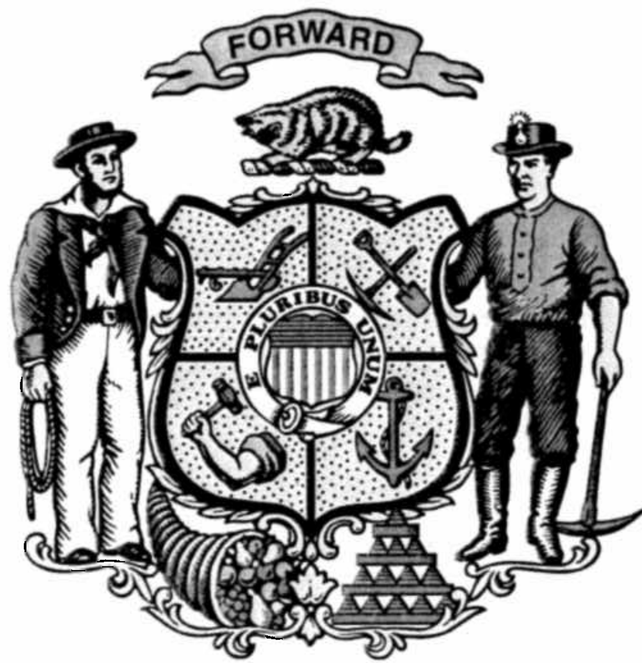
Attached to this memorandum are: (1) a summary of the Uniform Prudent Investor Act on which Assembly Bill 285 is based; and (2) the Uniform Prudent Investor Act, including the prefatory notes and comments.

As noted in the Act, it has been approved both by the National Conference of Commissioners on Uniform State Laws and by the American Bar Association. According to John McCabe, Director of the National Conference of Commissioners on Uniform State Laws, seven states: California, Colorado, New Mexico, Oklahoma, Oregon, Utah and Washington, have adopted the Act. In addition, according to Mr. McCabe, Illinois has adopted a law which is "substantially the same" as the Act.

If you have any questions or I can be of further assistance, please let me know.

GAA:jmm:ky;wu

Attachments


FORWARD
E PLURIBUS UNUM

State Representative
GREGG UNDERHEIM
Chair: Assembly Committee on Health

P.O. Box 8953, State Capitol
Madison, WI 53708-8953
(608) 266-2254

Legislative Hotline:
1 (800) 362-9472
(messages only)

1652 Beech Street,
Oshkosh, WI 54901
(414) 233-1082

Date: November 29, 1995

To: Representative Sheryl Albers, Chair
Assembly committee on Insurance, Securities
& Corporate Policy

From: Representative Gregg Underheim

Re: Assembly Committee Hearing 11/30/95

As related to your office yesterday, I will be unable to attend the Assembly committee on Insurance, Securities & Corporate Policy hearing on Thursday, November 30 at 1:00 P.M.

It is my understanding that an Executive Session may be held on AB 285. If I were in attendance for this hearing, I would vote "Yes" for AB 285.

Thank you for my "excused absence." Best wishes for a successful hearing.

GU:pkc

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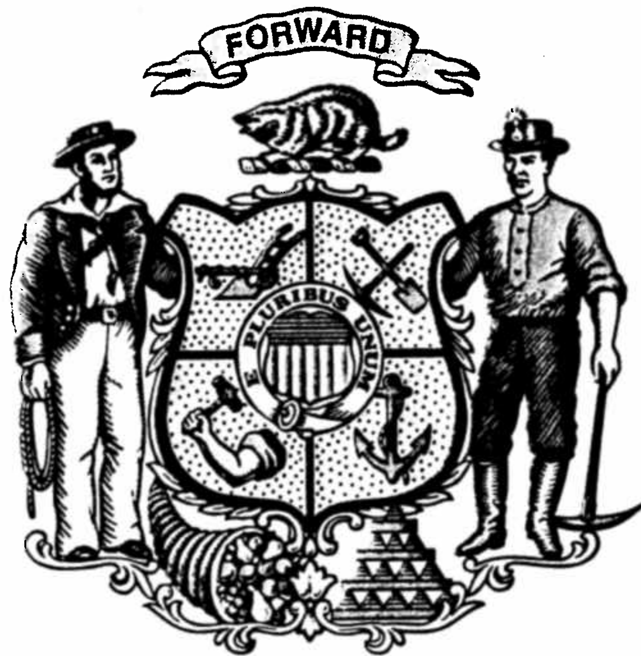
FORWARD
E PLURIBUS UNUM

Mary Hubler

State Representative

October 16, 1995

Representative Sheryl Albers
Chairperson
Assembly Committee on Insurance, Securities
and Corporate Policy
127 West - State Capitol
Madison, WI 53702

Dear Chairperson Albers:

I understand the Senate Committee on Insurance and the Assembly Committee on Insurance, Securities and Corporate Policy will hold a public hearing on October 19 on Assembly Bill 285, relating to regulating the investments of trustees.

Unfortunately, I am unable to attend the hearing, but have enclosed brief testimony as to why Wisconsin should adopt the Uniform Prudent Investor Act (AB 285). I would appreciate your sharing this testimony with the members of the joint committee.

Thank you. If you have any questions or if I can provide you or the committee with further information, please don't hesitate to contact me.

Sincerely,

Mary

MARY HUBLER
State Representative
75th Assembly District

MH/jms
enc.

Copy to Committee members

Office: State Capitol, P.O. Box 8952, Madison, WI 53708 • (608) 266-2519
Home: P.O. Box 544, Rice Lake, WI 54868 • (715) 234-7421
Toll-free Legislative Hotline • 1-800-362-9472

Mary Hubler

State Representative

TESTIMONY ON ASSEMBLY BILL 285
THE UNIFORM PRUDENT INVESTOR ACT

Assembly Bill 285 (The Uniform Prudent Investor Act) reverses common law rules that restrict the investment powers of trustees. Assembly Bill 285 requires a trustee to invest as a prudent investor would, using reasonable care, skill and caution in light of the objectives and risk tolerance of the individual trust. Diversification of assets is an obligation. Trustees can delegate investment responsibilities to experts. Within the scope of these powers and duties, trustees can choose to invest in any kind of asset that meets the objective of the specific trusts.

What are the specific advantages of Assembly Bill 285?

1. Trusts are likely to achieve a better return for beneficiaries than is the case under the common law rules.

2. Trustees can protect the trust corpus better through diversification of assets than is the case under the common law rules.

3. Trustees can invest to counter the effects of inflation, something that the common rules do not allow.

4. A trustee no longer is forced to rely upon his or her own knowledge and expertise, but can acquire investment services to enhance his or her own knowledge and skill.

5. Trustees can take into account the changing character and kinds of assets available for investment, free of archaic restrictions.

6. Trustees are judged on overall performance of the assets in a trust, rather than on the performance of specific assets.

7. The specific needs of each trust can be taken into account in devising investment strategy, rather than be subordinate to generic investment rules treating all trusts as the same.

8. Assembly Bill 285 will provide uniformity of law, necessary in interstate investment environment.

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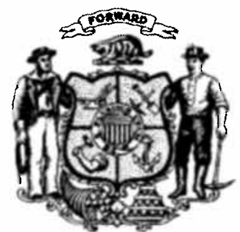
WISCONSIN STATE LEGISLATURE



A Few Facts About

THE UNIFORM PRUDENT INVESTOR ACT

PURPOSE: This act removes much of the common law restriction upon the investment authority of trustees of trusts and like fiduciaries. It allows such fiduciaries to utilize modern portfolio theory to guide investment decisions. A fiduciary's performance is measured on the performance of the whole portfolio, not upon the performance of each investment singly. The act allows the fiduciary to delegate investment decisions to qualified and supervised agents. It requires sophisticated risk-return analysis to guide investment decisions.

ORIGIN: Completed by the Uniform Law Commissioners in 1994.

ENDORSED BY: American Bar Association

STATE ADOPTIONS:

California *
Colorado *
New Mexico *
Oklahoma *
Oregon *
Utah *
Washington *

1995 INTRODUCTIONS:

Connecticut
Illinois

For any further information regarding the Uniform Prudent Investor Act, please contact John McCabe or Katie Robinson at 312-915-0195.

* 1995 Enactment

(9-1-95)

UNIFORM PRUDENT INVESTOR ACT

-A SUMMARY-

Trustees of trusts and like fiduciaries have been subject to rules severely restricting the types of investment modalities in which they can invest the assets of the trusts that they administer and manage. Interest-bearing instruments – safe income – of limited kinds (no junk bonds) are the limit of risk permitted or thought to be permitted under the traditional rules. Protect the paper value of the principal at all costs is the mandate for trustees. In addition, a trustee's performance is rated by the performance of each and every investment, singly, and not on the performance of the whole of the portfolio. And trustees have been precluded from obtaining professional investment help.

The result for trusts is modest income production at best without regard for the erosion of a trust's assets by inflation. Can it be that these rules miscalculate the real risk and actually jeopardize the assets of a trust rather than provide for their protection?

The answer is yes. And a remedy is now at hand in the Uniform Prudent Investor Act (UPIA), promulgated by the Uniform Law Commissioners in 1994. The adoption of this act by the state legislatures will correct the rules, based on false and damaging premises, that now govern the actions of trustees.

By no means does UPIA turn trustees into unrestrained speculators. It provides rules governing investment that, in fact, result in greater protection for the trust's assets while providing a prospect of better income. UPIA does not encourage irresponsible, speculative behavior, but requires careful assessment of investment goals, careful analysis of risk versus return, and diversification of assets to protect them. It gives the trustee the tools to accomplish these ends. UPIA requires trustees to become devotees of "modern portfolio theory" and to invest as a prudent investor would invest "considering the purposes, terms, distribution requirements, and other circumstances of the trust" using "reasonable care, skill, and caution."

The trustee has a list of factors which must be considered in making investment decisions, including "general economic conditions," "possible effect of inflation or deflation," "the expected total return from income and the appreciation of capital," and "other resources of the beneficiaries." The trustee must take tax consequences of investment decisions into account. There is a positive obligation to diversify assets "unless the trustee reasonably determines that, because of special circumstances, the purposes of the trust are better served without diversifying." The trustee's obligations are significant, requiring sophisticated approaches to investment that really take into account the right risk-to-return ratio for the particular trust.

In addition, a trustee's performance in UPIA is measured by the performance of all the assets together. A loss with respect to a single asset does not mean that the trustee has violated his or her fiduciary responsibilities. The act takes the truly holistic approach to investment practices.

In return for these obligations, UPIA removes any restrictions upon the types of investment modalities which may be chosen in a trust's portfolio. It is quite possible, for example, to hold positions in high-interest bonds (junk bonds) or mutual funds investing in such bonds, in a diversified portfolio, if such an investment meets the needs of the particular trust in light of the risk/return analysis specific to that trust.

One of the boons to trustees of smaller trusts is the ability to invest in mutual funds. Mutual funds reduce investment risk by diversifying their portfolios. By using mutual funds, a trustee of a trust that does not have a large enough corpus to effectively diversify its assets can enhance diversification of the trust's portfolio to limit the trust's risk of loss.

UPIA also permits the trustee to delegate investment and management functions "that a prudent trustee of comparable skills could properly delegate under the circumstances." Careful selection of the agent and careful, periodic review of the agent's actions are part of the trustee's responsibility when delegating authority. An agent has a responsibility of reasonable care in conducting the delegated business of the trust.

Why is it that the prudent man rule of prior law may, in fact, jeopardize the assets in a trust? Some of the instruments in which trustees have been able to invest have become more volatile in price. Treasury bonds, for example, long thought to be safe investments, now fluctuate considerably in value with the fluctuation of interest rates. The former so-called safe investment may not be so safe anymore. In contrast, common stocks have shown consistently better returns over the years than bonds – yet trustees have been prevented from investing in common stocks. Stocks have been historically safer investments, therefore, in diversified portfolios than bonds have been. Trusts have been deprived of return at some greater risk by the antiquated rules that govern investment of their assets.

By far the most insidious damage to trust assets comes from inflation. If trustees cannot invest in modalities that exceed the rate of inflation in return, the inevitable result is diminution of the corpus of the trusts they manage. The beneficiaries of trusts so restricted lose in all ways, both with respect to income and principal.

The UPIA provides rules that can be modified or waived in the trust agreement. Any person who wishes to put property in trust and who wants to provide different standards of conduct for the trustee is permitted to do so under UPIA.

UPIA provides a reasonable approach to the investment of trust assets that better meets the needs of beneficiaries while preserving trust assets. It should become the law in every state as soon as possible.

Founded in 1892, the National Conference of Commissioners on Uniform State Laws is a confederation of state commissioners on uniform laws. Its membership is comprised of 300 practicing lawyers, judges, and law professors who are appointed by each of the 50 states, the District of Columbia, Puerto Rico and the U.S. Virgin Islands to draft uniform and model state laws and work toward their enactment.

WHY STATES SHOULD ADOPT THE UNIFORM PRUDENT INVESTOR ACT

The Uniform Prudent Investor Act reverses common law rules that restrict the investment powers of trustees. The new act requires a trustee to invest as a prudent investor would, using reasonable care, skill and caution in light of the objectives and risk tolerance of the individual trust. Diversification of assets is an obligation. Trustees can delegate investment responsibilities to experts. Within the scope of these powers and duties, trustees can choose to invest in any kind of asset that meets the objective of the specific trust.

What are the specific advantages of the Uniform Prudent Investor Act?

1. Trusts are likely to achieve a better return for beneficiaries than is the case under the common law rules.

2. Trustees can protect the trust corpus better through diversification of assets than is the case under the common law rules.

3. Trustees can invest to counter the effects of inflation, something that the common rules do not allow.

4. A trustee no longer is forced to rely upon his or her own knowledge and expertise, but can acquire investment services to enhance his or her own knowledge and skill.

5. Trustees can take into account the changing character and kinds of assets available for investment, free of archaic restrictions.

6. Trustees are judged on overall performance of the assets in a trust, rather than on the performance of specific assets.

7. The specific needs of each trust can be taken into account in devising investment strategy, rather than be subordinate to generic investment rules treating all trusts as the same.

8. The Act will provide uniformity of law, necessary in an interstate investment environment.

❦

Philadelphia Legal Intelligencer
March 28, 1995

The Legal Intelligencer
BUSINESS LAW

TAX COUNSEL

Uniform Prudent Investor Act

What it Means to Your Trust

BY GERALD S. SUSMAN
Special to the Legal

When reviewing your estate plan, one important consideration is the selection of a trustee for any trust you might create. One responsibility a trustee has is to invest the trust assets for the benefit of the trust's designated beneficiaries. This creates an issue of how the trustee is to handle investment responsibilities.

The Uniform Prudent Investor Act, introduced in late 1994 by the National Conference of Commissioners on Uniform State Laws, is a model that most states will follow in the future. This act provides a new set of rules for trustees to be guided by when carrying out investment of trust assets.

For lawyers who draft trusts, the Uniform Act signals a warning to review all boilerplate provisions in existing trust forms dealing with the trustee's handling of investments. In many cases, existing trusts should be amended to conform with the new concepts introduced by the Uniform Act.

The Uniform Prudent Investor Act has several important features that differentiates it from the prudent investor rules of old:

Uniform Act

- Trustees judged on overall investment portfolio.
- Encourages trustee delegation to professionals.
- Emphasizes income and diversity in selection of investments.

Old Standard

- Trustees judged on individual investment performance.
- Delegation of investment responsibility technically improper.
- Emphasizes due care and prudence in selection of investments.

The Uniform Act signals a warning to review all boilerplate provisions in existing trust forms.

The importance of the Uniform Prudent Investor Act is to set a standard at which the beneficiaries of a trust as well as the trustee himself can judge whether the trustee has fulfilled his fiduciary role in investing the trust's assets.

At the present time, the Uniform Prudent Investor Act has been adopted in some form in 17 states (Alabama, California, Delaware, Florida, Georgia, Indiana, Illinois, Kansas, Minnesota, Montana, New Jersey, Nevada, New York, South Carolina, Tennessee, Virginia and Washington), the most recent being New Jersey.

In order to more fully appreciate the consequences of this act, we turn to look at the standards being applied presently in Pennsylvania.

Pennsylvania Statute

Pennsylvania has a Prudent Man Investor statute, but has not as of this date adopted the Uniform Act. See 20 PaCSA section 7302.

This law states that a trustee must exercise the degree of judgment and care, under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income to be derived therefrom as well as the probable safety of their capital.

Under this standard, a trustee's performance is measured by individual investments as opposed to the overall portfolio's performance.

The settlor of a trust may modify the trustee's role by delineating the powers, duties, and liabilities of the trustee regarding the investment or noninvestment of princi- [CONTINUED ON PAGE 10]

Gerald S. Susman, LL.M. (Tax), C.P.A., directs his practice towards the specialized tax needs of members of the bar, accountants and life underwriters. His book, Estate Planning, published by Law Journal Seminar-Press, is available by calling 1-800-888-8300, Ext. 565. Questions may be directed to him at Benjamin Franklin Business Center, 1515 Locust St., Suite 700, Philadelphia, Pa. 19102; telephone 731-1800.

Investor Act

[CONTINUED FROM P. 9]

pal and income, thereby potentially eliminating the effects of this statute entirely.

This may be desirable if the settlor's main concern is keeping the principal intact for some specified purpose as opposed to concerns that the trust reach its maximum income earning potential to provide support for the beneficiaries.

Like the older state statutes, the Uniform Prudent Investor Act may also ›e expanded, restricted, eliminated or ›therwise altered by the provisions of a rust.

This is particularly important to note ecause in states where this act has been dopted, it is retroactive and applies to rusts existing on and created after its ffective date.

Therefore, you should check the lanuage in your trust instrument to see if ıe act was invoked. If it is you may want › take action to amend your trust in der to exclude the effects of the act.

Invoking the Act

Terms that invoke the act in the trust clude, but are not limited to: "legal vestment," "authorized investments," rudent investor rule," or the particular language depicting the standard of that rule.

What this act means for a person creating a trust ("settlor") is that while he or she may have relied upon a state statute in defining more conservative investment standards for the trustee to follow, this new rule allows and even demands in some cases that a more aggressive strategy be followed.

On the other hand, under the old state statutes, a trustee may have felt secure knowing that his or her duties to the trust were being fulfilled by investing in any of the statute's authorized investments as long as he kept a watchful eye that the assets were not in any danger.

Under the new act, a trustee is responsible to diversify and generate income, not just maintain capital. Being a prudent investor is not enough. Many individuals are not knowledgeable enough to act as trustees in this capacity. The problem this brings to light is that people currently acting as trustees are responsible to rise up to this new standard.

Solutions

There are solutions for both the settlor and the trustee who are not comfortable with the ramifications of this act.

For a settlor, the answer may be to incorporate language into your trust so that the trustee cannot choose certain types of investments, thereby limiting his or her choice to more stable investments. Additionally, if maintaining the principal intact is your primary purpose then specify that as the primary obligation of the trustee.

For the trustee, the act states that a trustee may delegate investment and management functions that a prudent trustee of comparable skills could properly delegate under the circumstances.

In Florida, the statute imposes a responsibility to notify the beneficiaries in writing of such delegation. A trustee who delegates this responsibility will not be liable for poor performance by the investment manager if the delegation was reasonable.

The delegation should establish the scope and terms of the delegation consistent with the trust. Also, the trustee must periodically review the manager's actions in order to monitor the investment agent's performance and compliance with the terms of the trust.

Trustee not Liable

If these requirements are followed, the trustee will not be liable to the beneficiaries or to the trust for the decisions or actions of the agent to whom the function was delegated. However, the agent will generally be responsible to the beneficiaries if he or she fails to comply with the standards of this act.

It should be remembered that the purpose of the Uniform Prudent Investor Act is to bring the trustee up to the standards of the investment industry as a whole.

That is not to say that such standards comport to the goals of the trust. If they do, then the beneficiaries should be happy knowing that their best interests are being served. If they do not, then there are steps that can be taken to eliminate this standard from your trust.

Remember, the first step in determining whether you should be concerned is to review your instrument in order to see if the act was invoked when the trust was signed. You can take the necessary measures to include yourself under the act if it has been adopted in your state, or to exclude yourself if it does not help you reach your trust's goals.

* * *

Note: On Jan. 10, 1995, an article was published which identified the 80 percent limitation on meal and entertainment expenses as still being in effect. This was in error and it should be noted that the limitation is now 50 percent.

LAWYERS WEEKLY USA

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Trusts Are Being Reviewed

New Statutes Cause Lawyers to Revise Agreements

By Susan A. Cardoza

The responsibilities of trustees are being radically changed by new statutes that have been adopted in 16 states and are expected to sweep the rest of the country in the very near future, experts say.

The new requirements need to be considered by any lawyer who ever drafts a trust instrument, according to experts.

New York is the latest state to adopt a "prudent investor" statute. The New York law goes into effect on January 1.

There are two major changes:

◆ Investments will no longer be considered "prudent" just because each individual investment is safe. Rather, a trustee must formulate an overall investment strategy that takes into account general economic conditions, tax consequences, inflation, the needs of the beneficiaries and the duration of the trust.

◆ Investment responsibility can now be delegated to an

Continued on page 16

Photo by Ed Quinn

Trust drafters and trustees need to know about the new rules, says Mary Lehman. Otherwise, 'Someone could really get into trouble.'

Trusts Are Being Reviewed Because of New Statutes

Continued from page 1

outside expert.

This means that lawyers who are under the new statute will want to (1) reexamine their trust boilerplate and (2) advise clients that if they don't want a trustee to dabble in derivatives and junk bonds, they must say so specifically.

Lawyers should do this even in the 34 states that do not yet have such a statute, experts say, since it is expected that these states will quickly adopt one and current trust instruments need to be drafted with the new rules in mind.

In all states, the safest approach is to specify in the trust how the trustee should handle the investments, they add.

"Some clients may not want diversification or may strongly feel that the trust should be invested solely in government bonds," says Scottsdale, Arizona attorney Edward Lowry. "If that's the case, there will have to be specific language in the trust document saying so."

The new requirements "are a default rule, so a trust can change them explicitly," he says. "But most boilerplate language in trust documents doesn't contemplate this."

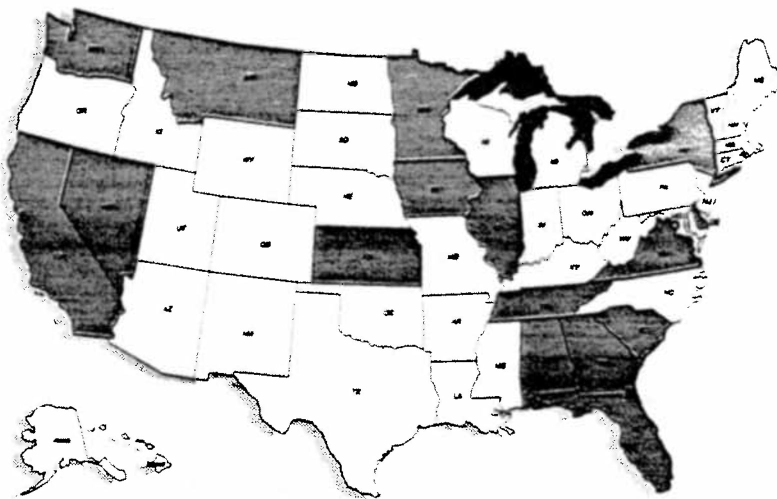
New York attorney Jonathan Bell warns, "You're not serving your clients well unless you revisit your forms.

"Clients have to be told that from now on, no investment will be considered by its nature inappropriate, no matter how speculative it is. If a client wants only AAA bond investments, they will have to say so explicitly."

The 16 state statutes contain a number of minor variations. However, last week the National Conference of Commissioners on Uniform State Laws completed a new "Uniform Prudent Investor Act" and recommended that every state enact it.

Eventually, all the states (including the ones that now have a similar statute) will fall into line with the Uniform Act, lawyers predict.

The States That Have Adopted the Statutes



ALABAMA: Ala. Code §19-3-120.2.
CALIFORNIA: Cal. Probate Code §16040.
DELAWARE: 12 Del. Code §3302.
FLORIDA: Fla. Stat. §518.11.
GEORGIA: Code of Ga. §53-8-2.
ILLINOIS: 760 Ill. Comp. Stat. 5/5.
IOWA: Iowa Code §633.123.
KANSAS: Kan. Stat. §17-5004.
MINNESOTA: Minn. Stat. §501B.10.
MONTANA: Mont. Code §72-34-114.
NEVADA: Nev. Rev. Stat. §164.050.
NEW YORK: N.Y. Estates, Powers and Trusts Law §11-2.3.
SOUTH CAROLINA: Code of Laws of S.C. §62-7-302.
TENNESSEE: Tenn. Code §35-3-117.
VIRGINIA: Code of Va. §26-45.1.
WASHINGTON: Code of Wash. §11.100.020.

No More 'Prudent Man'

The new statutes are a rejection of the old "prudent man rule," under which each individual investment was considered separately in determining whether the trustee had acted prudently.

Under the old rule, a trustee could be surcharged for a loss on one investment even if another one made money, says Lowry, who served on the Uniform Act's review committee.

But that's not how professional money managers do it, says Donna Barwick, who practices in Atlanta. "They look at the portfolio as a whole."

The new statutes reflect modern thinking about investments, says Barwick, by focusing on the methodology and not just on the particular type of investment.

Under the new rule, "A trustee has to put together an investment mix that will keep ahead of inflation," says New York attorney Mary Lehman, a managing director at Bankers Trust Company.

"You have to make money, not just maintain capital. And it has to be a diversified portfolio — you can't just play it safe and put all the money in Treasury bills. A lot of people aren't financially sophisticated enough to meet this standard, and you can't say, 'I'm just a lawyer. I did the best I could' any more."

With the total portfolio approach, no investment is per se imprudent. Rather, "A strategy that looks at the entire fund is required," says New York attorney Jerold Zieselman. The trustee is free to invest as he sees fit, keeping in mind the terms of the trust.

Lawyers who advise fiduciaries "need to tell them what liability they face and how they should diversify," says New York attorney Linda Hirschson.

According to Chicago attorney Joe Rubinelli, "Lawyers need to explain to their trustee clients that they no longer have to avoid certain investments because they are 'imprudent.'" On the other hand, "Trustees are now responsible for looking beyond traditional investments."

Liability for 'Imprudence'

Under the new rule, if a trustee is found to have acted imprudently, he or she is personally responsible for the amount by which the trust was damaged, says Lehman.

And this amount could be more than simply a loss of principal, says Zieselman. Arguably, under the new rules the damage to the trust could be the difference between "what the portfolio would have been worth if it had been invested prudently and what it is worth now."

On the other hand, the new rules are beneficial to trustees in that they focus on the trustee's conduct and not on the particular financial result, says Richard Wellman, a professor at the University of Georgia and a member of the Uniform Act's drafting committee.

"If a trustee formulates a diverse portfolio, he is not going to be liable," Wellman says. "To comply with the Act is a defense."

Zieselman agrees. "The trustee is protected even if there are losses. That's a big change."

The Act contains a number of factors that trustees should consider in developing a portfolio, although there is no strict requirement that they consider every single one of them.

"A failure to consider one factor is not necessarily imprudent, although all of them are indicative of prudence," says Wellman.

Delegating to Experts

The new rules encourage trustees to delegate investment responsibility to outside managers, says Zieselman.

A trustee who delegates this responsibility will not be liable for poor performance in most cases, so long as the delegation itself was reasonable.

This is "a major shift," says Boston estate planner Raymond Young.

In the past, delegation was technically improper. "You could get outside advice, but you couldn't delegate," says John Langbein, a professor at Yale Law School and a member of the committee that drafted the Uniform Act.

"This area had been unclear," agrees Lowry. "The new rule makes it explicit."

In practice, trustees have delegated investment responsibility for years, but they created "a fictional paper trail" to make it look like they weren't doing so because it technically breached the trust, says Bell.

Some of the 16 state statutes don't address the delegation issue. "The earlier state statutes are not as comprehensive," says Langbein. "But they will probably incorporate the Uniform Act over time."

What Should a Trustee Do?

Trustees should consider carefully whether they are financially savvy enough to meet the new standard, experts say.

"Someone could really get into trouble," warns Lehman.

Under the new rules, "Some people have no business serving as trustees because they don't know how to manage money," says Langbein. "But if you can't do brain surgery, you shouldn't do brain surgery — you should delegate to an outside expert. Now it's easier for trustees to do so, because the new rules welcome delegation."

In the past, many trustees would simply buy bonds — "the safe harbor for dumb trustees," says Wellman. "The problem is, that was murder on beneficiaries."

Barwick says it's "probably true" that not everyone has the financial skills to meet the new requirements. However, "It doesn't require a rocket scientist to invest in a mutual fund," she notes.

Trustees should determine what the proper investment strategy is "and document it in writing," says Lehman. "Ask the beneficiaries about their tolerance for risk. Do due diligence and document it. Then, if the world goes to hell, the trustee is protected."

Many trustees should "do themselves a favor" and get professional advice, Lehman says.

Is a 'Delegatee' Liable?

Generally, if a trustee delegates responsibility to an investment manager, the manager will be liable to the trust beneficiaries if anything goes wrong.

(Under the New York statute, a trustee may still be liable along with a "delegatee" even if the delegation was reasonable. But this is unusual, according to Bell.)

One thing that's not clear under the statutes is whether, if the trustee invests in a mutual fund, the mutual fund may be liable as a "delegatee."

"Just investing in a fund might be different from hiring an investment advisor," says Hirschson.

Bell says that he "can't imagine how a fiduciary could shift responsibility to a mutual fund. It's not usually thought of as a delegation."

Experts Like It

On the whole, experts say the new statutes are a positive development.

"They bring the standard to what it is in the market as a whole," says Wellman.

The total portfolio approach is "a lot better," says Lowry. "Nobody can be right 100% of the time."

Your Own Account/Mary Rowland

Avoiding Pitfalls of Trustees' Law

With more leeway in investing may come more vulnerability.

A LAW that takes effect in New York on Jan. 1 will give trustees far more leeway in managing money and will allow them to invest more aggressively in many cases. But the change could leave individual trustees and executors vulnerable to lawsuits.

Modeled in part after a law in Illinois and expected to be adopted by other states, the measure requires trustees to pursue an investment strategy that takes into account things like the risk and return of various investments, the impact of inflation and the general economic outlook. The old law was written in such a way that the biggest concern of trustees was preserving capital, not making sure the trust kept pace with inflation or its beneficiaries' needs.

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By making overall strategy more important than the performance of any individual investment, the law gives trustees great discretion.

Anyone put in charge of someone else's money should take heed, said Richard Rothberg, a partner in the New York law firm of Kronish, Lieb, Weiner & Hellman. "What this means is that if you don't at least consult a professional, you are taking your chances on being sued," he said. "It isn't enough just to buy bonds or put the money in the bank because it can be eroded by inflation."

Diversification becomes crucial as well. "You can't just hold everything in one investment," Mr. Rothberg said.

Felipe Galindo

In New York and most other states, anyone entrusted with managing another person's money must follow the "prudent man" rule. "This rule applies for a guardian for an infant, for a child who is appointed to take care of mom's affairs because she has Alzheimer's or for the doctor who is named executor of his friend's estate," Mr. Rothberg said.

If the trustee is sued by the beneficiaries, he must show he abided by the rule. Under the old New York law, a "prudent man" must invest with an eye toward "reasonable income and preservation of capital," explained John D. Dadakis, a partner at Rogers & Wells, a New York law firm.

During the last several years, the "preservation of capital" rule has been the subject of increasing criticism. For one thing, it stymies a trustee who wants to invest in stocks to keep pace with inflation, because the shares will fluctuate in value and could lead to an erosion of principal.

"What did preservation of capital mean?" Mr. Dadakis asked. "If you started with $100 and you maintained the trust at $100, was that preservation of capital?"

In most states, including New York, a trustee who loses money in any one investment can be sued. "The law measures the results of the trustee by performance rather than conduct," said Joshua Rubenstein, a partner in the New York law firm of Rosenman & Colin. "So if he triples the value of the portfolio but has a major loss in one security, he can be surcharged for that loss."

The rule about the preservation of capital also flies in the face of modern portfolio theory, which favors dividing investments among several types of assets with different risk and reward characteristics. Where possible, the assets will be chosen so that even in down markets some will hold up in value, helping to temper losses. With a modern portfolio approach, "you take into account not so much that everything you did worked out well," Mr. Dadakis said, "but that the strategy worked out well."

The National Council of Commissioners on Uniform State Laws in Chicago and the American Law Institute, an affiliate of the American Bar Association, have been working to change the prudent man rule. "This has been festering since the late 70's when high inflation ate into portfolio returns," Mr. Dadakis said.

A model law, the Uniform Prudent Investor Act, was introduced by the council in August, Mr. Rubenstein said. "Hopefully, it will catch on," he said.

The New York law, passed in July, instructs the trustee to "invest as a prudent investor looking for overall return," Mr. Dadakis said.

Though the responsible party must use care in overseeing portfolios, he will not be on the hook if one investment goes sour. "The new law says a certain standard of conduct is required as opposed to a certain outcome or performance," Mr. Rubenstein said. "It sets out nine factors that must be considered in making investments, so you now have a map in front of you and you can prove you have dealt with it responsibly."

Another change involves the ability to delegate money management. A restriction in the old law prevents trustees from delegating such authority — a matter of little significance to a bank trust department with extensive money management capabilities. But it is important for, say, a doctor who is executor of a friend's estate. "This is something that happens all the time," Mr. Rothberg said. "He is busy practicing medicine. How can he oversee the portfolio himself?" The new law permits delegation, but "it says you must monitor the investments and control the costs," he said. ■

THE NEW YORK TIMES **MONEY** SUNDAY, NOVEMBER 6, 1994

UNIFORM PRUDENT INVESTOR ACT

Drafted by the

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

and by it

APPROVED AND RECOMMENDED FOR ENACTMENT
IN ALL THE STATES

at its

ANNUAL CONFERENCE
MEETING IN ITS ONE-HUNDRED-AND-THIRD YEAR
IN CHICAGO, ILLINOIS
JULY 29 - AUGUST 5, 1994

WITH PREFATORY NOTE AND COMMENTS

Approved by the American Bar Association
Miami, Florida, February 14, 1995

UNIFORM PRUDENT INVESTOR ACT

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UNIFORM PRUDENT INVESTOR ACT

PREFATORY NOTE

Over the quarter century from the late 1960's the investment practices of fiduciaries experienced significant change. The Uniform Prudent Investor Act (UPIA) undertakes to update trust investment law in recognition of the alterations that have occurred in investment practice. These changes have occurred under the influence of a large and broadly accepted body of empirical and theoretical knowledge about the behavior of capital markets, often described as "modern portfolio theory."

This Act draws upon the revised standards for prudent trust investment promulgated by the American Law Institute in its Restatement (Third) of Trusts: Prudent Investor Rule (1992) [hereinafter Restatement of Trusts 3d: Prudent Investor Rule; also referred to as 1992 Restatement].

Objectives of the Act. UPIA makes five fundamental alterations in the former criteria for prudent investing. All are to be found in the Restatement of Trusts 3d: Prudent Investor Rule.

(1) The standard of prudence is applied to any investment as part of the total portfolio, rather than to individual investments. In the trust setting the term "portfolio" embraces all the trust's assets. UPIA § 2(b).

(2) The tradeoff in all investing between risk and return is identified as the fiduciary's central consideration. UPIA § 2(b).

(3) All categoric restrictions on types of investments have been abrogated; the trustee can invest in anything that plays an appropriate role in achieving the risk/return objectives of the trust and that meets the other requirements of prudent investing. UPIA § 2(e).

(4) The long familiar requirement that fiduciaries diversify their investments has been integrated into the definition of prudent investing. UPIA § 3.

(5) The much criticized former rule of trust law forbidding the trustee to delegate investment and management functions has been reversed. Delegation is now permitted, subject to safeguards. UPIA § 9.

Literature. These changes in trust investment law have been presaged in an extensive body of practical and scholarly writing. See especially the

discussion and reporter's notes by Edward C. Halbach, Jr., in Restatement of Trusts 3d: Prudent Investor Rule (1992); see also Edward C. Halbach, Jr., Trust Investment Law in the Third Restatement, 27 Real Property, Probate & Trust J. 407 (1992); Bevis Longstreth, Modern Investment Management and the Prudent Man Rule (1986); Jeffrey N. Gordon, The Puzzling Persistence of the Constrained Prudent Man Rule, 62 N.Y.U.L. Rev. 52 (1987); John H. Langbein & Richard A. Posner, The Revolution in Trust Investment Law, 62 A.B.A.J. 887 (1976); Note, The Regulation of Risky Investments, 83 Harvard L. Rev. 603 (1970). A succinct account of the main findings of modern portfolio theory, written for lawyers, is Jonathan R. Macey, An Introduction to Modern Financial Theory (1991) (American College of Trust & Estate Counsel Foundation). A leading introductory text on modern portfolio theory is R.A. Brealey, An Introduction to Risk and Return from Common Stocks (2d ed. 1983).

Legislation. Most states have legislation governing trust-investment law. This Act promotes uniformity of state law on the basis of the new consensus reflected in the Restatement of Trusts 3d: Prudent Investor Rule. Some states have already acted. California, Delaware, Georgia, Minnesota, Tennessee, and Washington revised their prudent investor legislation to emphasize the total-portfolio standard of care in advance of the 1992 Restatement. These statutes are extracted and discussed in Restatement of Trusts 3d: Prudent Investor Rule § 227, reporter's note, at 60-66 (1992).

Drafters in Illinois in 1991 worked from the April 1990 "Proposed Final Draft" of the Restatement of Trusts 3d: Prudent Investor Rule and enacted legislation that is closely modeled on the new Restatement. 760 ILCS § 5/5 (prudent investing); and § 5/5.1 (delegation) (1992). As the Comments to this Uniform Prudent Investor Act reflect, the Act draws upon the Illinois statute in several sections. Virginia revised its prudent investor act in a similar vein in 1992. Virginia Code § 2645.1 (prudent investing) (1992). Florida revised its statute in 1993. Florida Laws, ch. 93-257, amending Florida Statutes § 518.11 (prudent investing) and creating § 518.112 (delegation). New York legislation drawing on the new Restatement and on a preliminary version of this Uniform Prudent Investor Act was enacted in 1994. N.Y. Assembly Bill 11683-B, Ch. 609 (1994), adding Estates, Powers and Trusts Law § 11-2.3 (Prudent Investor Act).

Remedies. This Act does not undertake to address issues of remedy law or the computation of damages in trust matters. Remedies are the subject of a reasonably distinct body of doctrine. See generally Restatement (Second) of Trusts §§ 197-226A (1959) [hereinafter cited as Restatement of Trusts 2d; also referred to as 1959 Restatement].

Implications for charitable and pension trusts. This Act is centrally concerned with the investment responsibilities arising under the private gratuitous trust, which is the common vehicle for conditioned wealth transfer within the family. Nevertheless, the prudent investor rule also bears on charitable and pension trusts, among others. "In making investments of trust funds the trustee of a charitable trust is under a duty similar to that of the trustee of a private trust." Restatement of Trusts 2d § 389 (1959). The Employee Retirement Income Security Act (ERISA), the federal regulatory scheme for pension trusts enacted in 1974, absorbs trust-investment law through the prudence standard of ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a). The Supreme Court has said: "ERISA's legislative history confirms that the Act's fiduciary responsibility provisions 'codif[y] and mak[e] applicable to [ERISA] fiduciaries certain principles developed in the evolution of the law of trusts.'" *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 110-11 (1989) (footnote omitted).

Other fiduciary relationships. The Uniform Prudent Investor Act regulates the investment responsibilities of trustees. Other fiduciaries – such as executors, conservators, and guardians of the property – sometimes have responsibilities over assets that are governed by the standards of prudent investment. It will often be appropriate for states to adapt the law governing investment by trustees under this Act to these other fiduciary regimes, taking account of such changed circumstances as the relatively short duration of most executorships and the intensity of court supervision of conservators and guardians in some jurisdictions. The present Act does not undertake to adjust trust-investment law to the special circumstances of the state schemes for administering decedents' estates or conducting the affairs of protected persons.

Although the Uniform Prudent Investor Act by its terms applies to trusts and not to charitable corporations, the standards of the Act can be expected to inform the investment responsibilities of directors and officers of charitable corporations. As the 1992 Restatement observes, "the duties of the members of the governing board of a charitable corporation are generally similar to the duties of the trustee of a charitable trust." Restatement of Trusts 3d: Prudent Investor Rule § 379, Comment *b*, at 190 (1992). See also id. § 389, Comment *b*, at 190-91 (absent contrary statute or other provision, prudent investor rule applies to investment of funds held for charitable corporations).

UNIFORM PRUDENT INVESTOR ACT

SECTION 1. PRUDENT INVESTOR RULE.

(a) Except as otherwise provided in subsection (b), a trustee who invests and manages trust assets owes a duty to the beneficiaries of the trust to comply with the prudent investor rule set forth in this [Act].

(b) The prudent investor rule, a default rule, may be expanded, restricted, eliminated, or otherwise altered by the provisions of a trust. A trustee is not liable to a beneficiary to the extent that the trustee acted in reasonable reliance on the provisions of the trust.

Comment

This section imposes the obligation of prudence in the conduct of investment functions and identifies further sections of the Act that specify the attributes of prudent conduct.

Origins. The prudence standard for trust investing traces back to *Harvard College v. Amory*, 26 Mass. (9 Pick.) 446 (1830). Trustees should "observe how men of prudence, discretion and intelligence manage their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income, as well as the probable safety of the capital to be invested." Id. at 461.

Prior legislation. The Model Prudent Man Rule Statute (1942), sponsored by the American Bankers Association, undertook to codify the language of the *Amory* case. See Mayo A. Shattuck, The Development of the Prudent Man Rule for Fiduciary Investment in the United States in the Twentieth Century, 12 Ohio State L.J. 491, at 501 (1951); for the text of the model act, which inspired many state statutes, see id. at 508-09. Another prominent codification of the *Amory* standard is Uniform Probate Code § 7-302 (1969), which provides that "the trustee shall observe the standards in dealing with the trust assets that would be observed by a prudent man dealing with the property of another . . . ."

Congress has imposed a comparable prudence standard for the administration of pension and employee benefit trusts in the Employee Retirement Income Security Act (ERISA), enacted in 1974. ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a), provides that "a fiduciary shall discharge his duties with respect to a plan solely in the interest of the participants and beneficiaries and . . . with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent man acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of like character and with like aims . . . ."

Prior Restatement. The Restatement of Trusts 2d (1959) also tracked the language of the *Amory* case: "In making investments of trust funds the trustee is under a duty to the beneficiary . . . to make such investments and only such investments as a prudent man would make of his own property having in view the preservation of the estate and the amount and regularity of the income to be derived . . . ." Restatement of Trusts 2d § 227 (1959).

Objective standard. The concept of prudence in the judicial opinions and legislation is essentially relational or comparative. It resembles in this respect the "reasonable person" rule of tort law. A prudent trustee behaves as other trustees similarly situated would behave. The standard is, therefore, objective rather than subjective. Sections 2 through 9 of this Act identify the main factors that bear on prudent investment behavior.

Variation. Almost all of the rules of trust law are default rules, that is, rules that the settlor may alter or abrogate. Subsection (b) carries forward this traditional attribute of trust law. Traditional trust law also allows the beneficiaries of the trust to excuse its performance, when they are all capable and not misinformed. Restatement of Trusts 2d § 216 (1959).

SECTION 2. STANDARD OF CARE; PORTFOLIO STRATEGY; RISK AND RETURN OBJECTIVES.

(a) A trustee shall invest and manage trust assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution.

(b) A trustee's investment and management decisions respecting individual assets must be evaluated not in isolation but in the context of the trust portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust.

(c) Among circumstances that a trustee shall consider in investing and managing trust assets are such of the following as are relevant to the trust or its beneficiaries:

(1) general economic conditions;

(2) the possible effect of inflation or deflation;

(3) the expected tax consequences of investment decisions or strategies;

(4) the role that each investment or course of action plays within the overall trust portfolio, which may include financial assets, interests in closely held enterprises, tangible and intangible personal property, and real property;

(5) the expected total return from income and the appreciation of capital;

(6) other resources of the beneficiaries;

(7) needs for liquidity, regularity of income, and preservation or appreciation of capital; and

(8) an asset's special relationship or special value, if any, to the purposes of the trust or to one or more of the beneficiaries.

(d) A trustee shall make a reasonable effort to verify facts relevant to the investment and management of trust assets.

(e) A trustee may invest in any kind of property or type of investment consistent with the standards of this [Act].

(f) A trustee who has special skills or expertise, or is named trustee in reliance upon the trustee's representation that the trustee has special skills or expertise, has a duty to use those special skills or expertise.

Comment

Section 2 is the heart of the Act. Subsections (a), (b), and (c) are patterned loosely on the language of the Restatement of Trusts 3d: Prudent Investor Rule § 227 (1992), and on the 1991 Illinois statute, 760 § ILCS 5/5a (1992). Subsection (f) is derived from Uniform Probate Code § 7-302 (1969).

Objective standard. Subsection (a) of this Act carries forward the relational and objective standard made familiar in the *Amory* case, in earlier prudent investor legislation, and in the Restatements. Early formulations of the prudent person rule were sometimes troubled by the effort to distinguish between the standard of a prudent person investing for another and investing on his or her own account. The language of subsection (a), by relating the trustee's duty to "the purposes, terms, distribution requirements, and other circumstances of the trust," should put such questions to rest. The standard is the standard of the prudent investor similarly situated.

Portfolio standard. Subsection (b) emphasizes the consolidated portfolio standard for evaluating investment decisions. An investment that might be imprudent standing alone can become prudent if undertaken in sensible relation to other trust assets, or to other nontrust assets. In the trust setting the term "portfolio" embraces the entire trust estate.

Risk and return. Subsection (b) also sounds the main theme of modern investment practice, sensitivity to the risk/return curve. See generally the works cited in the Prefatory Note to this Act, under "Literature." Returns correlate strongly with risk, but tolerance for risk varies greatly with the financial and other circumstances of the investor, or in the case of a trust, with the purposes of the trust and the relevant circumstances of the beneficiaries. A trust whose main purpose is to support an elderly widow of modest means will

have a lower risk tolerance than a trust to accumulate for a young scion of great wealth.

Subsection (b) of this Act follows Restatement of Trusts 3d: Prudent Investor Rule § 227(a), which provides that the standard of prudent investing "requires the exercise of reasonable care, skill, and caution, and is to be applied to investments not in isolation but in the context of the trust portfolio and as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust."

Factors affecting investment. Subsection (c) points to certain of the factors that commonly bear on risk/return preferences in fiduciary investing. This listing is nonexclusive. Tax considerations, such as preserving the stepped up basis on death under Internal Revenue Code § 1014 for low-basis assets, have traditionally been exceptionally important in estate planning for affluent persons. Under the present recognition rules of the federal income tax, taxable investors, including trust beneficiaries, are in general best served by an investment strategy that minimizes the taxation incident to portfolio turnover. See generally Robert H. Jeffrey & Robert D. Arnott, Is Your Alpha Big Enough to Cover Its Taxes?, Journal of Portfolio Management 15 (Spring 1993).

Another familiar example of how tax considerations bear upon trust investing: In a regime of pass-through taxation, it may be prudent for the trust to buy lower yielding tax-exempt securities for high-bracket taxpayers, whereas it would ordinarily be imprudent for the trustees of a charitable trust, whose income is tax exempt, to accept the lowered yields associated with tax-exempt securities.

When tax considerations affect beneficiaries differently, the trustee's duty of impartiality requires attention to the competing interests of each of them.

Subsection (c)(8), allowing the trustee to take into account any preferences of the beneficiaries respecting heirlooms or other prized assets, derives from the Illinois act, 760 ILCS § 5/5(a)(4) (1992).

Duty to monitor. Subsections (a) through (d) apply both to investing and managing trust assets. "Managing" embraces monitoring, that is, the trustee's continuing responsibility for oversight of the suitability of investments already made as well as the trustee's decisions respecting new investments.

Duty to investigate. Subsection (d) carries forward the traditional responsibility of the fiduciary investor to examine information likely to bear importantly on the value or the security of an investment – for example, audit

reports or records of title. E.g., *Estate of Collins*, 72 Cal. App. 3d 663, 139 Cal. Rptr. 644 (1977) (trustees lent on a junior mortgage on unimproved real estate, failed to have land appraised, and accepted an unaudited financial statement; held liable for losses).

Abrogating categoric restrictions. Subsection 2(e) clarifies that no particular kind of property or type of investment is inherently imprudent. Traditional trust law was encumbered with a variety of categoric exclusions, such as prohibitions on junior mortgages or new ventures. In some states legislation created so-called "legal lists" of approved trust investments. The universe of investment products changes incessantly. Investments that were at one time thought too risky, such as equities, or more recently, futures, are now used in fiduciary portfolios. By contrast, the investment that was at one time thought ideal for trusts, the long-term bond, has been discovered to import a level of risk and volatility – in this case, inflation risk – that had not been anticipated. Accordingly, section 2(e) of this Act follows Restatement of Trusts 3d: Prudent Investor Rule in abrogating categoric restrictions. The Restatement says: "Specific investments or techniques are not per se prudent or imprudent. The riskiness of a specific property, and thus the propriety of its inclusion in the trust estate, is not judged in the abstract but in terms of its anticipated effect on the particular trust's portfolio." Restatement of Trusts 3d: Prudent Investor Rule § 227, Comment f, at 24 (1992). The premise of subsection 2(e) is that trust beneficiaries are better protected by the Act's emphasis on close attention to risk/return objectives as prescribed in subsection 2(b) than in attempts to identify categories of investment that are per se prudent or imprudent.

The Act impliedly disavows the emphasis in older law on avoiding "speculative" or "risky" investments. Low levels of risk may be appropriate in some trust settings but inappropriate in others. It is the trustee's task to invest at a risk level that is suitable to the purposes of the trust.

The abolition of categoric restrictions against types of investment in no way alters the trustee's conventional duty of loyalty, which is reiterated for the purposes of this Act in Section 5. For example, were the trustee to invest in a second mortgage on a piece of real property owned by the trustee, the investment would be wrongful on account of the trustee's breach of the duty to abstain from self-dealing, even though the investment would no longer automatically offend the former categoric restriction against fiduciary investments in junior mortgages.

Professional fiduciaries. The distinction taken in subsection (f) between amateur and professional trustees is familiar law. The prudent investor standard applies to a range of fiduciaries, from the most sophisticated professional investment management firms and corporate fiduciaries, to family

members of minimal experience. Because the standard of prudence is relational, it follows that the standard for professional trustees is the standard of prudent professionals; for amateurs, it is the standard of prudent amateurs. Restatement of Trusts 2d § 174 (1959) provides: "The trustee is under a duty to the beneficiary in administering the trust to exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property; and if the trustee has or procures his appointment as trustee by representing that he has greater skill than that of a man of ordinary prudence, he is under a duty to exercise such skill." Case law strongly supports the concept of the higher standard of care for the trustee representing itself to be expert or professional. See Annot., Standard of Care Required of Trustee Representing Itself to Have Expert Knowledge or Skill, 91 A.L.R. 3d 904 (1979) & 1992 Supp. at 48-49.

The Drafting Committee declined the suggestion that the Act should create an exception to the prudent investor rule (or to the diversification requirement of Section 3) in the case of smaller trusts. The Committee believes that subsections (b) and (c) of the Act emphasize factors that are sensitive to the traits of small trusts; and that subsection (f) adjusts helpfully for the distinction between professional and amateur trusteeship. Furthermore, it is always open to the settlor of a trust under Section 1(b) of the Act to reduce the trustee's standard of care if the settlor deems such a step appropriate. The official comments to the 1992 Restatement observe that pooled investments, such as mutual funds and bank common trust funds, are especially suitable for small trusts. Restatement of Trusts 3d: Prudent Investor Rule § 227, Comments *h*, *m*, at 28, 51; reporter's note to Comment *g*, id. at 83.

Matters of proof. Although virtually all express trusts are created by written instrument, oral trusts are known, and accordingly, this Act presupposes no formal requirement that trust terms be in writing. When there is a written trust instrument, modern authority strongly favors allowing evidence extrinsic to the instrument to be consulted for the purpose of ascertaining the settlor's intent. See Uniform Probate Code § 2-601 (1990), Comment; Restatement (Third) of Property: Donative Transfers (Preliminary Draft No. 2, ch. 11, Sept. 11, 1992).

SECTION 3. DIVERSIFICATION. A trustee shall diversify the investments of the trust unless the trustee reasonably determines that, because of special circumstances, the purposes of the trust are better served without diversifying.

Comment

The language of this section derives from Restatement of Trusts 2d § 228 (1959). ERISA insists upon a comparable rule for pension trusts. ERISA § 404(a)(1)(C), 29 U.S.C. § 1104(a)(1)(C). Case law overwhelmingly supports the duty to diversify. See Annot., Duty of Trustee to Diversify Investments, and Liability for Failure to Do So, 24 A.L.R. 3d 730 (1969) & 1992 Supp. at 78-79.

The 1992 Restatement of Trusts takes the significant step of integrating the diversification requirement into the concept of prudent investing. Section 227(b) of the 1992 Restatement treats diversification as one of the fundamental elements of prudent investing, replacing the separate section 228 of the Restatement of Trusts 2d. The message of the 1992 Restatement, carried forward in Section 3 of this Act, is that prudent investing ordinarily requires diversification.

Circumstances can, however, overcome the duty to diversify. For example, if a tax-sensitive trust owns an underdiversified block of low-basis securities, the tax costs of recognizing the gain may outweigh the advantages of diversifying the holding. The wish to retain a family business is another situation in which the purposes of the trust sometimes override the conventional duty to diversify.

Rationale for diversification. "Diversification reduces risk . . . [because] stock price movements are not uniform. They are imperfectly correlated. This means that if one holds a well diversified portfolio, the gains in one investment will cancel out the losses in another." Jonathan R. Macey, An Introduction to Modern Financial Theory 20 (American College of Trust and Estate Counsel Foundation, 1991). For example, during the Arab oil embargo of 1973, international oil stocks suffered declines, but the shares of domestic oil producers and coal companies benefitted. Holding a broad enough portfolio allowed the investor to set off, to some extent, the losses associated with the embargo.

Modern portfolio theory divides risk into the categories of "compensated" and "uncompensated" risk. The risk of owning shares in a mature and well-managed company in a settled industry is less than the risk of owning shares in a start-up high-technology venture. The investor requires a higher expected return to induce the investor to bear the greater risk of disappointment associated with the start-up firm. This is compensated risk – the firm pays the investor for bearing the risk. By contrast, nobody pays the investor for owning too few stocks. The investor who owned only international oils in 1973 was running a risk that could have been reduced by having

configured the portfolio differently – to include investments in different industries. This is uncompensated risk – nobody pays the investor for owning shares in too few industries and too few companies. Risk that can be eliminated by adding different stocks (or bonds) is uncompensated risk. The object of diversification is to minimize this uncompensated risk of having too few investments. "As long as stock prices do not move exactly together, the risk of a diversified portfolio will be less than the average risk of the separate holdings." R.A. Brealey, An Introduction to Risk and Return from Common Stocks 103 (2d ed. 1983).

There is no automatic rule for identifying how much diversification is enough. The 1992 Restatement says: "Significant diversification advantages can be achieved with a small number of well-selected securities representing different industries . . . . Broader diversification is usually to be preferred in trust investing," and pooled investment vehicles "make thorough diversification practical for most trustees." Restatement of Trusts 3d: Prudent Investor Rule § 227, General Note on Comments *e-h*, at 77 (1992). See also Macey, supra, at 23-24; Brealey, supra, at 111-13.

Diversifying by pooling. It is difficult for a small trust fund to diversify thoroughly by constructing its own portfolio of individually selected investments. Transaction costs such as the round-lot (100 share) trading economies make it relatively expensive for a small investor to assemble a broad enough portfolio to minimize uncompensated risk. For this reason, pooled investment vehicles have become the main mechanism for facilitating diversification for the investment needs of smaller trusts.

Most states have legislation authorizing common trust funds; see 3 Austin W. Scott & William F. Fratcher, The Law of Trusts § 227.9, at 463-65 n.26 (4th ed. 1988) (collecting citations to state statutes). As of 1992, 35 states and the District of Columbia had enacted the Uniform Common Trust Fund Act (UCTFA) (1938), overcoming the rule against commingling trust assets and expressly enabling banks and trust companies to establish common trust funds. 7 Uniform Laws Ann. 1992 Supp. at 130 (schedule of adopting states). The Prefatory Note to the UCTFA explains: "The purposes of such a common or joint investment fund are to diversify the investment of the several trusts and thus spread the risk of loss, and to make it easy to invest any amount of trust funds quickly and with a small amount of trouble." 7 Uniform Laws Ann. 402 (1985).

Fiduciary investing in mutual funds. Trusts can also achieve diversification by investing in mutual funds. See Restatement of Trusts 3d: Prudent Investor Rule, § 227, Comment *m*, at 99-100 (1992) (endorsing trust investment in mutual funds). ERISA § 401(b)(1), 29 U.S.C. § 1101(b)(1),

expressly authorizes pension trusts to invest in mutual funds, identified as securities "issued by an investment company registered under the Investment Company Act of 1940 . . . ."

SECTION 4. DUTIES AT INCEPTION OF TRUSTEESHIP. Within a reasonable time after accepting a trusteeship or receiving trust assets, a trustee shall review the trust assets and make and implement decisions concerning the retention and disposition of assets, in order to bring the trust portfolio into compliance with the purposes, terms, distribution requirements, and other circumstances of the trust, and with the requirements of this [Act].

Comment

Section 4, requiring the trustee to dispose of unsuitable assets within a reasonable time, is old law, codified in Restatement of Trusts 3d: Prudent Investor Rule § 229 (1992), lightly revising Restatement of Trusts 2d § 230 (1959). The duty extends as well to investments that were proper when purchased but subsequently become improper. Restatement of Trusts 2d § 231 (1959). The same standards apply to successor trustees, see Restatement of Trusts 2d § 196 (1959).

The question of what period of time is reasonable turns on the totality of factors affecting the asset and the trust. The 1959 Restatement took the view that "[o]rdinarily any time within a year is reasonable, but under some circumstances a year may be too long a time and under other circumstances a trustee is not liable although he fails to effect the conversion for more than a year." Restatement of Trusts 2d § 230, comment *b* (1959). The 1992 Restatement retreated from this rule of thumb, saying, "No positive rule can be stated with respect to what constitutes a reasonable time for the sale or exchange of securities." Restatement of Trusts 3d: Prudent Investor Rule § 229, comment *b* (1992).

The criteria and circumstances identified in Section 2 of this Act as bearing upon the prudence of decisions to invest and manage trust assets also pertain to the prudence of decisions to retain or dispose of inception assets under this section.

SECTION 5. LOYALTY. A trustee shall invest and manage the trust assets solely in the interest of the beneficiaries.

Comment

The duty of loyalty is perhaps the most characteristic rule of trust law, requiring the trustee to act exclusively for the beneficiaries, as opposed to acting for the trustee's own interest or that of third parties. The language of Section 4 of this Act derives from Restatement of Trusts 3d: Prudent Investor Rule § 170 (1992), which makes minute changes in Restatement of Trusts 2d § 170 (1959).

The concept that the duty of prudence in trust administration, especially in investing and managing trust assets, entails adherence to the duty of loyalty is familiar. ERISA § 404(a)(1)(B), 29 U.S.C. § 1104(a)(1)(B), extracted in the Comment to Section 1 of this Act, effectively merges the requirements of prudence and loyalty. A fiduciary cannot be prudent in the conduct of investment functions if the fiduciary is sacrificing the interests of the beneficiaries.

The duty of loyalty is not limited to settings entailing self-dealing or conflict of interest in which the trustee would benefit personally from the trust. "The trustee is under a duty to the beneficiary in administering the trust not to be guided by the interest of any third person. Thus, it is improper for the trustee to sell trust property to a third person for the purpose of benefitting the third person rather than the trust." Restatement of Trusts 2d § 170, comment *q*, at 371 (1959).

No form of so-called "social investing" is consistent with the duty of loyalty if the investment activity entails sacrificing the interests of trust beneficiaries – for example, by accepting below-market returns – in favor of the interests of the persons supposedly benefitted by pursuing the particular social cause. See, e.g., John H. Langbein & Richard Posner, Social Investing and the Law of Trusts, 79 Michigan L. Rev. 72, 96-97 (1980) (collecting authority). For pension trust assets, see generally Ian D. Lanoff, The Social Investment of Private Pension Plan Assets: May it Be Done Lawfully under ERISA?, 31 Labor L.J. 387 (1980). Commentators supporting social investing tend to concede the overriding force of the duty of loyalty. They argue instead that particular schemes of social investing may not result in below-market returns. See, e.g., Marcia O'Brien Hylton, "Socially Responsible" Investing: Doing Good Versus Doing Well in an Inefficient Market, 42 American U.L. Rev. 1 (1992). In 1994 the Department of Labor issued an Interpretive Bulletin reviewing its prior analysis of social investing questions and reiterating that pension trust fiduciaries may invest only in conformity with the prudence and

loyalty standards of ERISA §§ 403-404. Interpretive Bulletin 94-1, 59 Fed. Regis. 32606 (Jun. 22, 1994), to be codified as 29 CFR § 2509.94-1. The Bulletin reminds fiduciary investors that they are prohibited from "subordinat[ing] the interests of participants and beneficiaries in their retirement income to unrelated objectives."

SECTION 6. IMPARTIALITY. If a trust has two or more beneficiaries, the trustee shall act impartially in investing and managing the trust assets, taking into account any differing interests of the beneficiaries.

Comment

The duty of impartiality derives from the duty of loyalty. When the trustee owes duties to more than one beneficiary, loyalty requires the trustee to respect the interests of all the beneficiaries. Prudence in investing and administration requires the trustee to take account of the interests of all the beneficiaries for whom the trustee is acting, especially the conflicts between the interests of beneficiaries interested in income and those interested in principal.

The language of Section 6 derives from Restatement of Trusts 2d § 183 (1959); see also id., § 232. Multiple beneficiaries may be beneficiaries in succession (such as life and remainder interests) or beneficiaries with simultaneous interests (as when the income interest in a trust is being divided among several beneficiaries).

The trustee's duty of impartiality commonly affects the conduct of investment and management functions in the sphere of principal and income allocations. This Act prescribes no regime for allocating receipts and expenses. The details of such allocations are commonly handled under specialized legislation, such as the Revised Uniform Principal and Income Act (1962) (which is presently under study by the Uniform Law Commission with a view toward further revision).

SECTION 7. INVESTMENT COSTS. In investing and managing trust assets, a trustee may only incur costs that are appropriate and reasonable in relation to the assets, the purposes of the trust, and the skills of the trustee.

Comment

Wasting beneficiaries' money is imprudent. In devising and implementing strategies for the investment and management of trust assets, trustees are obliged to minimize costs.

The language of Section 7 derives from Restatement of Trusts 2d § 188 (1959). The Restatement of Trusts 3d says: "Concerns over compensation and other charges are not an obstacle to a reasonable course of action using mutual funds and other pooling arrangements, but they do require special attention by a trustee. . . . [I]t is important for trustees to make careful cost comparisons, particularly among similar products of a specific type being considered for a trust portfolio." Restatement of Trusts 3d: Prudent Investor Rule § 227, comment *m*, at 58 (1992).

SECTION 8. REVIEWING COMPLIANCE. Compliance with the prudent investor rule is determined in light of the facts and circumstances existing at the time of a trustee's decision or action and not by hindsight.

Comment

This section derives from the 1991 Illinois act, 760 ILCS 5/5(a)(2) (1992), which draws upon Restatement of Trusts 3d: Prudent Investor Rule § 227, comment *b*, at 11 (1992). Trustees are not insurers. Not every investment or management decision will turn out in the light of hindsight to have been successful. Hindsight is not the relevant standard. In the language of law and economics, the standard is ex ante, not ex post.

SECTION 9. DELEGATION OF INVESTMENT AND MANAGEMENT FUNCTIONS.

(a) A trustee may delegate investment and management functions that a prudent trustee of comparable skills could properly delegate under the circumstances. The trustee shall exercise reasonable care, skill, and caution in:

(1) selecting an agent;

(2) establishing the scope and terms of the delegation, consistent with the purposes and terms of the trust; and

(3) periodically reviewing the agent's actions in order to monitor the agent's performance and compliance with the terms of the delegation.

(b) In performing a delegated function, an agent owes a duty to the trust to exercise reasonable care to comply with the terms of the delegation.

(c) A trustee who complies with the requirements of subsection (a) is not liable to the beneficiaries or to the trust for the decisions or actions of the agent to whom the function was delegated.

(d) By accepting the delegation of a trust function from the trustee of a trust that is subject to the law of this State, an agent submits to the jurisdiction of the courts of this State.

Comment

This section of the Act reverses the much-criticized rule that forbad trustees to delegate investment and management functions. The language of this section is derived from Restatement of Trusts 3d: Prudent Investor Rule § 171 (1992), discussed infra, and from the 1991 Illinois act, 760 ILCS § 5/5.1(b), (c) (1992).

Former law. The former nondelegation rule survived into the 1959 Restatement: "The trustee is under a duty to the beneficiary not to delegate to others the doing of acts which the trustee can reasonably be required personally to perform." The rule put a premium on the frequently arbitrary task of distinguishing discretionary functions that were thought to be nondelegable from supposedly ministerial functions that the trustee was allowed to delegate. Restatement of Trusts 2d § 171 (1959).

The Restatement of Trusts 2d admitted in a comment that "There is not a clear-cut line dividing the acts which a trustee can properly delegate from those which he cannot properly delegate." Instead, the comment directed attention to a list of factors that "may be of importance: (1) the amount of

discretion involved; (2) the value and character of the property involved; (3) whether the property is principal or income; (4) the proximity or remoteness of the subject matter of the trust; (5) the character of the act as one involving professional skill or facilities possessed or not possessed by the trustee himself." Restatement of Trusts 2d § 171, comment *d* (1959). The 1959 Restatement further said: "A trustee cannot properly delegate to another power to select investments." Restatement of Trusts 2d § 171, comment *h* (1959).

For discussion and criticism of the former rule see William L. Cary & Craig B. Bright, The Delegation of Investment Responsibility for Endowment Funds, 74 Columbia L. Rev. 207 (1974); John H. Langbein & Richard A. Posner, Market Funds and Trust-Investment Law, 1976 American Bar Foundation Research J. 1, 18-24.

The modern trend to favor delegation. The trend of subsequent legislation, culminating in the Restatement of Trusts 3d: Prudent Investor Rule, has been strongly hostile to the nondelegation rule. See John H. Langbein, Reversing the Nondelegation Rule of Trust-Investment Law, 59 Missouri L. Rev. 105 (1994).

The delegation rule of the Uniform Trustee Powers Act. The Uniform Trustee Powers Act (1964) effectively abrogates the nondelegation rule. It authorizes trustees "to employ persons, including attorneys, auditors, investment advisors, or agents, even if they are associated with the trustee, to advise or assist the trustee in the performance of his administrative duties; to act without independent investigation upon their recommendations; and instead of acting personally, to employ one or more agents to perform any act of administration, whether or not discretionary . . . ." Uniform Trustee Powers Act § 3(24), 7B Uniform Laws Ann. 743 (1985). The Act has been enacted in 16 states, see "Record of Passage of Uniform and Model Acts as of September 30, 1993," 1993-94 Reference Book of Uniform Law Commissioners (unpaginated, following page 111) (1993).

UMIFA's delegation rule. The Uniform Management of Institutional Funds Act (1972) (UMIFA), authorizes the governing boards of eleemosynary institutions, who are trustee-like fiduciaries, to delegate investment matters either to a committee of the board or to outside investment advisors, investment counsel, managers, banks, or trust companies. UMIFA § 5, 7A Uniform Laws Ann. 705 (1985). UMIFA has been enacted in 38 states, see "Record of Passage of Uniform and Model Acts as of September 30, 1993," 1993-94 Reference Book of Uniform Law Commissioners (unpaginated, following page 111) (1993).

ERISA's delegation rule. The Employee Retirement Income Security Act of 1974, the federal statute that prescribes fiduciary standards for investing the assets of pension and employee benefit plans, allows a pension or employee benefit plan to provide that "authority to manage, acquire or dispose of assets of the plan is delegated to one or more investment managers . . . ." ERISA § 403(a)(2), 29 U.S.C. § 1103(a)(2). Commentators have explained the rationale for ERISA's encouragement of delegation:

> ERISA . . . invites the dissolution of unitary trusteeship. . . . ERISA's fractionation of traditional trusteeship reflects the complexity of the modern pension trust. Because millions, even billions of dollars can be involved, great care is required in investing and safekeeping plan assets. Administering such plans – computing and honoring benefit entitlements across decades of employment and retirement – is also a complex business . . . . Since, however, neither the sponsor nor any other single entity has a comparative advantage in performing all these functions, the tendency has been for pension plans to use a variety of specialized providers. A consulting actuary, a plan administration firm, or an insurance company may oversee the design of a plan and arrange for processing benefit claims. Investment industry professionals manage the portfolio (the largest plans spread their pension investments among dozens of money management firms).

John H. Langbein & Bruce A. Wolk, Pension and Employee Benefit Law 496 (1990).

The delegation rule of the 1992 Restatement. The Restatement of Trusts 3d: Prudent Investor Rule (1992) repeals the nondelegation rule of Restatement of Trusts 2d § 171 (1959), extracted supra, and replaces it with substitute text that reads:

> § 171. Duty with Respect to Delegation. A trustee has a duty personally to perform the responsibilities of trusteeship except as a prudent person might delegate those responsibilities to others. In deciding whether, to whom, and in what manner to delegate fiduciary authority in the administration of a trust, and thereafter in supervising agents, the trustee is under a duty to the beneficiaries to exercise fiduciary discretion and to act as a prudent person would act in similar circumstances.

Restatement of Trusts 3d: Prudent Investor Rule § 171 (1992). The 1992 Restatement integrates this delegation standard into the prudent investor rule of section 227, providing that "the trustee must . . . act with prudence in deciding whether and how to delegate to others . . . ." Restatement of Trusts 3d: Prudent Investor Rule § 227(c) (1992).

Protecting the beneficiary against unreasonable delegation. There is an intrinsic tension in trust law between granting trustees broad powers that facilitate flexible and efficient trust administration, on the one hand, and protecting trust beneficiaries from the misuse of such powers on the other hand. A broad set of trustees' powers, such as those found in most lawyer-drafted instruments and exemplified in the Uniform Trustees' Powers Act, permits the trustee to act vigorously and expeditiously to maximize the interests of the beneficiaries in a variety of transactions and administrative settings. Trust law relies upon the duties of loyalty and prudent administration, and upon procedural safeguards such as periodic accounting and the availability of judicial oversight, to prevent the misuse of these powers. Delegation, which is a species of trustee power, raises the same tension. If the trustee delegates effectively, the beneficiaries obtain the advantage of the agent's specialized investment skills or whatever other attributes induced the trustee to delegate. But if the trustee delegates to a knave or an incompetent, the delegation can work harm upon the beneficiaries.

Section 9 of the Uniform Prudent Investor Act is designed to strike the appropriate balance between the advantages and the hazards of delegation. Section 9 authorizes delegation under the limitations of subsections (a) and (b). Section 9(a) imposes duties of care, skill, and caution on the trustee in selecting the agent, in establishing the terms of the delegation, and in reviewing the agent's compliance.

The trustee's duties of care, skill, and caution in framing the terms of the delegation should protect the beneficiary against overbroad delegation. For example, a trustee could not prudently agree to an investment management agreement containing an exculpation clause that leaves the trust without recourse against reckless mismanagement. Leaving one's beneficiaries remediless against willful wrongdoing is inconsistent with the duty to use care and caution in formulating the terms of the delegation. This sense that it is imprudent to expose beneficiaries to broad exculpation clauses underlies both federal and state legislation restricting exculpation clauses, e.g., ERISA §§ 404(a)(1)(D), 410(a), 29 U.S.C. §§ 1104(a)(1)(D), 1110(a); New York Est. Powers Trusts Law § 11-1.7 (McKinney 1967).

Although subsection (c) of the Act exonerates the trustee from personal responsibility for the agent's conduct when the delegation satisfies the standards of subsection 9(a), subsection 9(b) makes the agent responsible to the trust. The beneficiaries of the trust can, therefore, rely upon the trustee to enforce the terms of the delegation.

Costs. The duty to minimize costs that is articulated in Section 7 of this Act applies to delegation as well as to other aspects of fiduciary investing.

In deciding whether to delegate, the trustee must balance the projected benefits against the likely costs. Similarly, in deciding how to delegate, the trustee must take costs into account. The trustee must be alert to protect the beneficiary from "double dipping." If, for example, the trustee's regular compensation schedule presupposes that the trustee will conduct the investment management function, it should ordinarily follow that the trustee will lower its fee when delegating the investment function to an outside manager.

SECTION 10. LANGUAGE INVOKING STANDARD OF [ACT]. The following terms or comparable language in the provisions of a trust, unless otherwise limited or modified, authorizes any investment or strategy permitted under this [Act]: "investments permissible by law for investment of trust funds," "legal investments," "authorized investments," "using the judgment and care under the circumstances then prevailing that persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital," "prudent man rule," "prudent trustee rule," "prudent person rule," and "prudent investor rule."

Comment

This provision is taken from the Illinois act, 760 ILCS § 5/5(d) (1992), and is meant to facilitate incorporation of the Act by means of the formulaic language commonly used in trust instruments.

SECTION 11. APPLICATION TO EXISTING TRUSTS. This [Act] applies to trusts existing on and created after its effective date. As applied to trusts existing on its effective date, this [Act] governs only decisions or actions occurring after that date.

SECTION 12. UNIFORMITY OF APPLICATION AND CONSTRUCTION. This [Act] shall be applied and construed to effectuate its general purpose to make uniform the law with respect to the subject of this [Act] among the States enacting it.

SECTION 13. SHORT TITLE. This [Act] may be cited as the "[Name of Enacting State] Uniform Prudent Investor Act."

SECTION 14. SEVERABILITY. If any provision of this [Act] or its application to any person or circumstance is held invalid, the invalidity does not affect other provisions or applications of this [Act] which can be given effect without the invalid provision or application, and to this end the provisions of this [Act] are severable.

SECTION 15. EFFECTIVE DATE. This [Act] takes effect . . . .

SECTION 16. REPEALS. The following acts and parts of acts are repealed:

(1)

(2)

(3)

hours – amounting in some cases to millions of dollars worth of time – to the development of uniform and model acts. No state could afford the bills for the legal expertise that is donated to the drafting of uniform state laws.

PROCEDURES

Each uniform law is years in the making. The process starts with the Scope and Program Committee, which initiates the agenda of the Conference. It investigates each proposed act, and then reports to the Executive Committee whether a subject is one in which it is desirable and feasible to draft a uniform law. If the Executive Committee approves a recommendation, a drafting committee of commissioners is appointed. Drafting committees meet throughout the year. Tentative drafts are not submitted to the entire Conference until they have received extensive committee consideration.

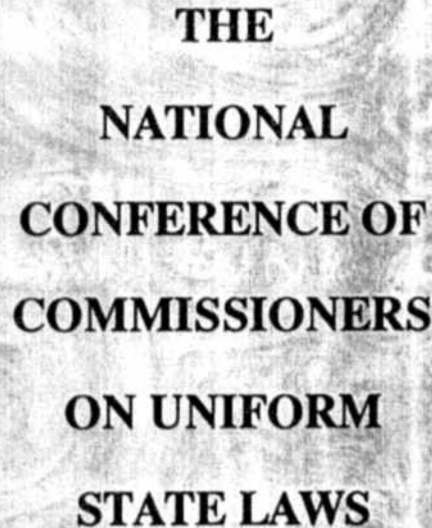
Draft acts are then submitted for initial debate of the entire Conference at an annual meeting. Each act must be considered section by section, at no less than two annual meetings by all commissioners sitting as a Committee of the Whole. With hundreds of trained eyes probing every concept and word, it is a rare draft that leaves an annual meeting in the same form it was initially presented.

Once the Committee of the Whole approves an act, its final test is a vote by states – one vote per state. A majority of the states present, and no less than 20 states, must approve an act before it can be officially adopted as a Uniform or Model Act.

At that point, a Uniform or Model Act is officially promulgated for consideration by the states. Legislatures are urged to adopt Uniform Acts exactly as written, to "promote uniformity in law among the several states." Model Acts are designed to serve as guideline legislation, which states can borrow from or adapt to suit their individual needs and conditions.

When drafting is completed on an act, a commissioner's work has only begun. They advocate the adoption of uniform and model acts in their home states. Normal resistance to anything "new" makes this the hardest part of a commissioner's job. But the result can be workable modern state law that helps keep the federal system alive.

The work of the Conference simplifies the legal life of businesses and individuals by providing rules and procedures that are consistent from state to state. Representing both state government and the legal profession, it is a genuine confederation of state interests. It has sought to bring uniformity to the divergent legal traditions of more than 50 sovereign jurisdictions, and has done so with significant success.



THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS

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ORGANIZATION

The National Conference of Commissioners on Uniform State Laws has worked for the uniformity of state laws since 1892. It is a non-profit unincorporated association, comprised of state commissions on uniform laws from each state, the District of Columbia, the Commonwealth of Puerto Rico and the U.S. Virgin Islands. Each jurisdiction determines the method of appointment and the number of commissioners actually appointed. Most jurisdictions provide for their commission by statute.

There is only one fundamental requirement for the more than 300 uniform law commissioners: that they be members of the bar in the jurisdiction they represent. While some commissioners serve as state legislators, most are practitioners, judges and law professors. They serve for specific terms, and receive no salaries or fees for their work with the Conference.

The state uniform law commissions come together as the National Conference for one purpose – to study and review the law of the states to determine which areas of law should be uniform. The commissioners promote the principle of uniformity by drafting and proposing specific statutes in areas of the law where uniformity between the states is desirable. It must be emphasized that the Conference can only propose – no uniform law is effective until a state legislature adopts it.

The Conference is a working organization. The uniform law commissioners participate in drafting specific acts; they discuss, consider and amend drafts of other commissioners; they decide whether to recommend an act as a uniform or a model act; and they work toward enactment of Conference acts in their home jurisdictions.

HISTORY

The uniform law movement began in the latter half of the 19th century. The Alabama State Bar Association recognized as early as 1881 the legal tangles created by wide variations in state laws. But it was not until 1889 that the American Bar Association decided, at its 12th Annual Meeting, to work for "uniformity of the laws" in the then 44 states.

Within a year, the New York Legislature authorized the governor to appoint three commissioners to explore the best way to effect uniformity of law between increasingly interdependent states. The ABA endorsed New York's action. The result was the first meeting of the *Conference of State Boards of Commissioners on Promoting Uniformity of Law in the U.S.*

Seven states sent commissioners to that first meeting of the Conference in Saratoga Springs, New York in 1892. By 1912, every state had appointed uniform law commissioners. The U.S. Virgin Islands is the last jurisdiction to join, appointing its first commission in 1988.

Since its organization, the Conference has drafted more than 200 uniform laws on numerous subjects and in various fields of law, setting patterns for uniformity across the nation. Uniform acts include the Uniform Probate Code, the Uniform Child Custody Jurisdiction Act, the Uniform Partnership Act, the Uniform Anatomical Gift Act and the Uniform Limited Partnership Act.

Most significant was the 1940 Conference decision to attack major commercial problems with comprehensive legal solutions – a decision that set in motion the project to produce the Uniform Commercial Code. The Code took ten years to complete and another 14 years before it was enacted across the country. It remains the signature product of the Conference.

Today the Conference is recognized primarily for its work in commercial law, family law, probate and estates, law of business organizations, health law, and conflicts of law. It rarely drafts law that is regulatory in character.

FINANCIAL SUPPORT

The major portion of financial support for the Conference comes from state appropriations. Expenses are apportioned among the states by means of an assessment based on population.

The Conference gets maximum results from minimum budgets because its major asset, drafting expertise, is donated. The only compensation for commissioners is the satisfaction derived from solving important legal problems. Commissioners devote hundreds and even thousands of