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Navigating the Responsibilities of Nonprofit Fiduciaries

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Fiduciaries to nonprofit organizations play an instrumental role in managing an organization's interests while furthering its important mission. However, the role of a fiduciary involves much more than attendance at meetings. Fiduciaries must exercise integrity, thoughtfulness and prudence in decision-making, all while being proactively engaged and asking the right questions. It's crucial that individuals undertaking the important responsibility of supervising a nonprofit's investments recognize that they are doing so in a fiduciary capacity and understand exactly what this entails.

What is a Fiduciary?

Simply explained, a fiduciary is a person or organization legally and ethically bound to act for the benefit of another party. In the case of a nonprofit, the fiduciary must always prioritize the best interests of the organization, ahead of the interests of board and committee members, or the interests of any others. This level of care is both legally and ethically binding, and disregard or even irresponsible execution of one's fiduciary responsibilities may result in personal liability for negligence.

Serving as a fiduciary to a nonprofit requires knowledge of investment issues and an understanding of how investment-related decisions may impact the organization. An individual is a fiduciary to the extent they exercise their discretionary authority and control over portfolio management or over the management or disposition of assets. Fiduciaries could include boards of directors, investment committee members and investment advisors of nonprofits.

Three Key Fiduciary Responsibilities

There are three key duties nonprofit fiduciaries are required to uphold under most state laws – duty of care, duty of loyalty and duty of obedience. These critical duties are summarized below:

1) **Duty of Care:** A fiduciary must act with reasonable and prudent care, skill and diligence when making decisions on behalf of the organization. A fiduciary should be an excellent steward of the organization's assets and resources, protecting them through a commitment to moral, ethical and rational financial decision-making. To help fulfill this duty, fiduciaries must make every effort to attend meetings, stay informed by monitoring budget and financial reports and remain engaged in strategic planning.

2) **Duty of Loyalty:** A fiduciary must act solely in the nonprofit's best interest and is forbidden to use the relationship with the organization to advantage themselves, their families and friends, or any others. Maintaining this duty of loyalty forms a bond of trust. Fiduciaries are required to disclose any potential conflicts of interest to the organizations they support and must seek to avoid these conflicts whenever possible.

3) **Duty of Obedience:** A fiduciary must ensure that the nonprofit's charitable mission and objectives are being carried out and that interested parties are adhering to the governing documents of the organization. This includes diverting the organization away from potentially competing or outlying interests, as well as making sure the nonprofit is complying with all applicable laws and regulations. It goes without saying that a fiduciary should not engage in illegal or unethical activities and take all steps possible to deter the nonprofit from such activities as well.

Guidance offered by the Uniform Prudent Management of Institutional Funds Act

To assist in identifying fiduciary responsibilities, the National Conference of Commissioners on Uniform State Laws created the Uniform Prudent Management of Institutional Funds Act ("UPMIFA") in July of 2006[1]. UPMIFA governs the management of funds donated to charitable institutions. Additionally, UPMIFA provides guidance and authority concerning the investment management and endowment expenditures of charitable institutions. UPMIFA has been adopted by most states since its development; however, it is considered to be a "model act," which means that each state can modify the proposed UPMIFA provisions, depending on local laws and regulations[2].

In terms of investment requirements, UPMIFA guidelines support duty of care in reinforcing that:

- Investments should be made in good faith and with the care an ordinary prudent person in a like position would exercise.
- Prudence should be taken in incurring investment costs, authorizing "only costs that are appropriate and reasonable."
- Investment decisions must be made by considering the fund's entire portfolio, and risk and return objectives should be reasonably suited to the fund and the institution. No investment decision should be made in isolation.

Spending rules outlined through UPMIFA relate specifically to endowment funds that are subject to donor restrictions. The goal for some endowments is to last until an objective(s) is met, while other endowments are intended to last in perpetuity.

UPMIFA outlines the following areas of consideration to help guide nonprofit fiduciaries in developing annual spending decisions:

- Duration and preservation of the portfolio(s)
- Purposes of the institution and the portfolio(s)
- General economic conditions
- Possible effect of inflation or deflation
- Expected total return from income and the appreciation of investments
- Other resources of the institution
- Investment policy of the institution

How Can Organizations Comply with UPMIFA?

Failure to comply with UPMIFA can result in monetary penalties, legal actions, loss of the nonprofit's tax-exempt status and reputational harm; however, there are ways that fiduciaries can help satisfy compliance and avoid these potentially serious consequences, including the following:

- Identify the organization's long-term objectives and unique needs through a comprehensive written Investment Policy Statement which will serve as the blueprint for how the investments will be overseen.
- Establish a formal spending policy and review it regularly to ensure it continues to meet the needs of the organization.
- Form a strong and active Investment Committee and provide ongoing educational opportunities so that members are fully aware of their fiduciary responsibilities.
- Hire a reputable advisor to manage the investment portfolio and help ensure that this advisor accepts its fiduciary responsibility (many agree to this in writing) and will be held accountable to the Committee.

[1] *Source: NACUBO; Uniform Prudent Management of Institutional Funds Act, February 2009*
[2] *Source: Rebeka Mazzone, The Uniform Prudent Management of Institutional Funds Act, Nonprofit Fiscal Fitness Newsletter, July 2009*

- Regularly monitor performance results and make changes as needed through establishing a comprehensive governance calendar.

Documenting investment decisions and the rationale behind them as well as sound governance practices both serve as additional protection for nonprofit fiduciaries. We welcome you to watch our brief video, *Creating Your Fiduciary Trail® with Fiducient Advisors*, to learn more.

Fiducient Advisors assists nonprofit organizations and committees/boards in establishing a robust fiduciary governance process. We help clients construct custom investment strategies to meet their objectives and goals while serving as a resource for our clients on a broad variety of topics, including fiduciary responsibility. We understand that our work must help advance our clients' missions, as investing for the benefit of others has never been more important. Therefore, we commit to helping boards, committees and staff perform as responsible financial stewards for the organizations they care about most. Whatever the objectives, we view ourselves as our clients' "strategic partner," striving to help achieve their goals with less time, cost and burden.

If you would like more information, contact any of the professionals at Fiducient Advisors.

About the Author

Kerry Elsass, CAIA®
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Kerry services institutional clients by providing counsel and guidance on portfolio design, asset allocation, manager selection, investment policy statements and overall performance monitoring. Prior to joining the firm in 2021, Kerry was a Principal and Senior Consultant with Mercer. She graduated from Miami University with a BS in Chemistry and received her MBA in Finance with Distinction from DePaul University Kellstadt Graduate School of Business. Additionally, she is a Chartered Alternative Investment Analyst (CAIA®) and a member of Chicago Women Investment Professionals. Kerry is a huge animal lover and enjoys traveling, reading and recently joined a social Bocce ball league.