November 4, 1971

Board of Trustees
The Trustees of the University
of Pennsylvania
3400 Walnut Street
Philadelphia, Pennsylvania 19104

Gentlemen:

You have asked our opinion, as University counsel, on whether the Trustees of the University may properly determine to apply to the reduction of the University's bank indebtedness a substantial amount of funds which the University has previously segregated and invested pending their eventual use for particular designated purposes.

The monies in question have been pooled for investment and are referred to as the Temporary Investments Fund (the "T.I.F."). As of June 30, the aggregate amount involved was in excess of $20,000,000. The source of most of these funds may be divided into three major categories, and it is only funds derived from these particular sources which are dealt with in this opinion:

1. The first major category of funds, totalling, as of June 30, about $7,000,000, are donations to the University accompanied by express or implied directions that the funds given are to be used to finance the construction of a building.

(1) We are not dealing here with the University's permanent endowment funds which are held in the Associated Investments Fund (the "A.I.F.").
2. The second major category of funds is accumulated income from endowments and other invested funds held for special purposes, totalling, as of June 30, about $2,000,000. Examples are income to support a particular chair where the chair has not yet been filled, income earmarked for uses such as research or archaeological expeditions or the like, that are scheduled to take place in the future.

3. The third category, totalling, as of June 30, about $11,000,000, are what are known as "restricted current funds" -- donations made to the University to defray the cost of carrying on particular University operations or projects in the future, similar to those referred to in the preceding paragraph, except that here principal as well as income may be used.

The T.I.F., totalling, as above indicated, as of June 30, about $20,000,000, has been kept invested, the average rate of return being about 5% per annum. At the same time, the University has outstanding loans with various banks of about $20,000,000. The cost of maintaining these loans is about 8% per annum. Your current concern is whether you may reduce these loans by using the monies currently in the T.I.F., thus improving not only the "return" by approximately 3%, but also the University's general credit rating.

You have advised us that there is nothing in any of the documents accompanying the gifts of the funds here under discussion stating specifically that they are to be held "in trust" or are to be used for no other purposes than that expressed in the terms of the gift.

In addition, it is our understanding that the Trustees, before making a determination to apply funds in the T.I.F. to reduce the University's bank borrowings, will satisfy themselves that the University will be in a position, when the terms of the gifts mature, to secure the funds necessary to meet its obligations as set forth in the donative instruments involved. Indeed, we have been advised that the authority...
given to the financial officers of the University to use funds from the T.I.F. to pay down bank debt will be conditioned by a requirement directing them to institute procedures which will insure that there is available to the University at all times, either in the T.I.F. or as the unused portion of established lines of bank credit, an amount equal to the sum of all funds which the University is from time to time obligated to expend for particular purposes. "Cash flow" projections indicating the funds required and their source will be kept, and the University will limit future bank borrowings as necessary to insure that its unused lines of credit are sufficient for the unfunded portion of these commitments.

The cases and authorities have long struggled with the problem of the nature of funds held by a charitable corporation, i.e. whether the funds are held "in trust" (2) or "quasi-in-trust" or "on condition" or the like, but the real question is what is the basic duty and obligation of the University with respect to such funds. This duty and obligation is found in the presumed intent of the donor. We believe that in making a gift to the University to be used for a specific purpose, the donor intends first that the specified purpose be carried out by the University at the appropriate time, and second that in the meantime, the University be so administered that when the appropriate time arrives the University will be in a position, financially and otherwise, to carry out the purpose.

Therefore, while the basic duty of the University with respect to funds involved in the T.I.F. is an undertaking that an amount equal to the sum mandated by the grantor will be used for the purpose indicated at the appropriate time, this undertaking is accompanied by an equally important duty to manage the University's fiscal affairs, including the actual funds given, in a manner which, so far as possible, will effectively insure that the purposes in question can be carried out by the University.

(2) A conclusion that contributions to a building fund, for instance, were actually impressed with a trust might well be inconsistent with the almost universal practice of large eleemosynary organizations to mortgage their buildings and improvements to secure borrowings from financial institutions.
The substantial difference in the return being earned on the T.I.F. and the interest cost to the University for borrowed money, the fact that the University, though confident of its essential financial stability and continued existence and operation is currently faced with continuing operating deficits, and the possibility that a failure to reduce its bank debt substantially might impair the University's credit standing and its eligibility for the prime rate on its bank borrowing furnish abundant ground for a determination by the Trustees that the application of T.I.F. funds to the reduction of bank debt at this time is a sounder and in effect "more prudent" use than their continued investment in debt securities.

While the question is one on which we have found no controlling judicial precedent, it is our opinion that a determination by the Trustees to use a portion of the funds in the T.I.F. in the manner envisioned in this letter would be sustained by the courts in any case involving a complaint against individual Trustees of the University alleging participation in a breach of trust.

Very truly yours,

DRINKER BIDDLE & REATH

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