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Senate Finance Committee
The Honorable Delores G. Kelley
3 East Miller Senate Building
Annapolis, Maryland 21401-1991

RE: SB 192 – Cemeteries – Perpetual Care – Distribution from Perpetual Care Trust Fund

Dear Chairman Kelley and Members of the Committee:

This bill will make an important change to existing law so our regulated cemeteries in Maryland can continue to be properly maintained in the future.

Maryland law does not currently regulate cemeteries owned and operated by churches or synagogues or other non-profit organizations, and this bill does not apply to them. But there are 89 cemeteries in Maryland that are operated by cemetery companies and that are subject to State regulation. These regulated cemeteries are each required to deposit 10% of the selling price of each cemetery lot into a perpetual care trust fund, and it is from such trust funds that the money is derived to maintain the cemeteries. It is very important that these funds are sufficient because if they are not, these cemeteries will lack essential maintenance and will fall into disrepair.

Currently, Maryland law provides that the “income” from a perpetual care trust fund shall be used for the perpetual care of the cemetery. For reasons that I will explain, this “income” standard is old-fashioned and inadequate.

The “income” standard provides that the principal of a trust fund cannot be touched and that the beneficiaries of the trust fund can only withdraw the “income” of the fund. But the “income” standard leads to two ways of administering a trust fund that inevitably will seriously impair the long-term viability of the fund. First, in order to maximize “income”, the trust fund trustee will tend to invest in securities that generate the most income. These securities tend to be fixed income securities such as bonds, which pay higher income each year than most stocks. But the higher income comes at a price. If you invest $20,000 in a 20 year bond today, at the end of the 20th year, you only receive your $20,000 back; the money hasn’t grown. And if you then re-invest the $20,000 in another 20 year bond, at the end of that 20th year, you again only receive your $20,000 back. In a world in which inflation causes the cost of living to rise each year, you can see how a system that induces the trustees of perpetual care trust funds to invest the fund principal in fixed income securities will over time strap cemetery owners of the money that they require to properly maintain the cemeteries. And then comes the second problem. As the income produced by a trust fund's investment in fixed income securities becomes inadequate to pay for a cemetery's maintenance, the fund trustee will be tempted to invest in more risky investments with higher payoffs. This policy might work for a time, but more risky investments are by definition *more risky,* and at some point, it is likely that the principal of the trust fund will be impaired or lost altogether.

Recognizing the deficiencies of using the "income" standard, many years ago, the nation's leading foundations and its university endowments, hospital endowments and other endowments shifted to a different standard of investing known as the "total return" standard. This standard is not in the least bit exotic or unusual. I am a member of an Episcopal church in downtown Baltimore. Our church endowment is invested pursuant to the "total return" standard. I am also on the board of a charitable foundation that annually donates about $700,000 to Baltimore City non-profits which benefit underprivileged children. Our endowment is invested pursuant to the "total return" standard. And finally, when my parents passed away and left their money in trust for my brother and me, we used the provisions of Maryland's existing estates and trusts law to invest the money of my parents' trust pursuant to the "total return" standard.

SB 192 will allow a regulated Maryland cemetery to either select the "income" or the "total return" method of distributing money from the cemetery's perpetual care trust fund. If the cemetery were to choose the "total return" method, the trustee would compute the end-of-year fair market value of the trust fund principal for each of the past three years, take the average and then distribute to the cemetery up to 4% of that average periodically during the following year to be used for cemetery maintenance. It is critical to note here that SB 192 explicitly provides that such a distribution may **only** be used for cemetery maintenance, repair and administrative purposes. Not a single dime of such distributions will find its way into the pockets of the cemetery's owners.

The advantage of the "total return" method is that it will encourage the fund trustees to invest fund assets in a balanced way in some securities that will pay current income but also in securities expected to pay little current income but rather to appreciate in value over the years. It is that appreciation in the value of the fund principal that will enable cemeteries over time to be able to cope with inflationary pressures and have enough money available to continue to pay for the proper maintenance of the cemetery as the decades pass. SB 192 further provides that all realized capital gains of a perpetual care trust fund "shall be deposited in the perpetual care trust fund as principal of the perpetual care trust fund." Once again, therefore, SB 192 makes it clear that the owner of the cemetery will not profit from the investment of some of the fund's assets in growth stocks.

I have attached to this testimony several documents showing the dramatic growth of the U. S. stock market over the past 100 years. In particular, there are two charts that show that, with only brief interruptions, the stock market has steadily risen. In a broadly diversified portfolio, the past hundred years of stock market results suggests that the value of the portfolio will grow as the years pass.

SB 192 places serious additional restrictions on cemeteries that choose to adopt the “total return” method. In such cases, the fund’s trustee must adopt an investment policy that supports the growth of the fund. Secondly, if the market value of the fund’s principal in any year is under 80% of the three year rolling average, the distribution will revert to the “income” method for that year. Thirdly, the fund must provide to the Office of Cemetery Oversight financial information for the past 5-7 years, and if the Director should conclude that the performance of the fund during the period in which the “total return” method applied has not resulted in sufficient protection of the fund’s principal, the Director may limit or prohibit a distribution. In these ways, SB 192 bends over backwards to protect the principal of perpetual care trust funds while permitting fund trustees, in the exercise of their fiduciary duties, to invest the fund’s assets so that they will grow over time.

I hope that the Finance Committee will carefully consider SB 192 and stand ready to answer any questions once my other witnesses have had a chance to make their presentations.